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A Study of Colorado's TABOR Law and Its Influence on Public Finance During the 2001 Recession

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A STUDY OF COLORADO'S TABOR LAW AND ITS INFLUENCE ON PUBLIC FINANCE DURING THE 2001 RECESSION

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ABSTRACT

Colorado's constitutional Taxpayer Bill of Rights (TABOR) is a product of the citizen initiative process, a mechanism of direct democracy that allows citizens to circumvent legislatures and enact laws themselves. A prominent argument against this process is that such a mode of lawmaking can generate conflicts within state constitutions and bring about unintended consequences. This paper considers the Colorado state budget difficulties that arose during the 2001 recession, the relationship of TABOR and those difficulties, and finds that TABOR resulted in unintended consequences that were unforeseen by voters who approved the measure. Examples of these unanticipated, unintended consequences include: significant budget cuts for higher education, reductions in state mental health services, and insufficiencies within the TABOR law regarding how TABOR refunds were to be made.

Table of Contents

1. Introduction

1.1 Overview of the 2001-05 Recession

Proponents of Colorado's TABOR law laud it as an effective instrument for constraining government growth since it links allowable government revenue collection with population growth and inflation. The policy implications of restricting government growth in Colorado to such measures were intensely disputed between 2001 and 2005. Aggregate state revenue declines, paired with the requirements of Colorado's numerous tax and expenditure limitations (TELs), led to numerous budget complications.

At the onset, capital projects were halted, hiring for state jobs was sharply curtailed, and operational spending was scaled back. But this was not enough, and as the recession worsened, so did the condition of the state budget. The situation was dire by the beginning of the 2002 regular session.

To further complicate matters, officials could not be sure how long poor economic conditions would persist, and no comprehensive fix to the predicament was put forth. Consequently, rather than an intentional, systematic approach, measures to address the crisis desperately unfolded in a piecemeal fashion. For each fiscal year, officials took whatever actions were necessary to balance the budget and maintain core operations, while, with limited information, also planning for the next fiscal year. Between FY 2000-01 and FY 2004-05, the budgets of fifteen departments were reduced. The most substantial budget cuts overall were to Transportation and Human Services, for which total funding was reduced by 34.1% and 6.6% respectively. The greatest proportional reduction in General Fund allocation was for Higher Education, which contributed to tuition increases, among other consequences

1.2 Colorado Tax and Expenditure Limitations and the Recession

The citizen initiative process allows citizens to place policy measures on electoral ballots for voter consideration which then become law if approved by popular vote. The process is therefore a mechanism of direct democracy since it allows citizens to bypass the legislature—a process that is highly controversial. Most research on the subject of direct democracy in the United States has focused generally on the implications of the initiative process for public policy, and, within this context, has emphasized three subject areas: the use of the process to achieve policy outcomes both directly and indirectly; voter competence and the preferences of voters when making such policy decisions; and how direct democracy affects the interests of minority groups since the process transforms the will of the majority into law.

Tax and expenditure limitations (TELs) are measures that restrain government growth by restricting allowable government revenue collection, spending levels, or both. Colorado's TABOR Amendment, enacted in 1992, is a tax and expenditure limitation that originated as a citizen initiative. State population growth and the inflation rate are the two elements of the TABOR formula that dictates how much collected revenue the state may retain each year. In theory, those are the two key factors that are needed in determining how much revenue the state needs in order to maintain a "same level of services" budget from year to year, which is the source of the notion that the formula allows government growth to keep pace with the economy.

However, many state departments are caseload driven, and thus their budget needs vary with the number of cases. A common criticism raised in the literature is that the budget needs of departments can exceed the allowable TABOR growth limit, which is especially important for departments that provide services to vulnerable populations (e.g., "State"). From calendar year 2001-03, the TABOR formula permitted the state government to grow by 12.9 percent. To the extent that some departments of the state experienced budget growth rates below 12.9 percent over this period, while simultaneously experiencing caseload growth above the growth rate of the general population, it is not unreasonable to argue that services delivered to clients or citizens were reduced; budget growth rates below 12.9% between 2001 and 2003, coupled with increased caseload demand, indicate service reductions ("State" 9).

1.3 Motivation

Significant aspects of governance and public finance are within the purview of TABOR, which, coupled with its exceptional degree of restrictiveness, makes an understanding of TABOR's consequences indispensable. The central assertion in this paper is that Colorado's TABOR Amendment had unintended consequences that became apparent during the recession. This paper emphasizes the budget cuts made to mental health services, higher education. Also emphasized are ambiguities in the TABOR law regarding exact surplus refund mechanisms.

While there exist numerous studies that offer assessments of TABOR, impressions of it remain assorted. The Cato Institute suggests that all states should adopt the Colorado model. Former Colorado Governor Bill Owens, in a 2003 *Wall Street Journal* editorial, argued that TABOR had been a catalyst of unprecedented growth in the

1990s, and that California's Governor, Arnold Schwarzenegger, should adopt a similar approach to address his state's deficit (Martell and Teske 673). In contrast, the Center on Budget and Policy Priorities suggests that, "What has happened in Colorado should be a cautionary tale for any other state considering going down the TABOR path. Services deteriorated to the point at which the quality of life in the state has been undermined, and the state's potential for economic development has been weakened" (Bradley and Lyons). During the 2001 recession, twenty-eight states had tax and expenditure limitations, and activity in other states suggests that the further enactment of TELs is likely.

2. A Survey of Tax and Expenditure Limitations

2.1 Overview of Initiatives, Referenda, and Direct Democracy

While this paper does not specifically consider the effects of the initiative process on minority interests in Colorado, this section is intended to provide a broad overview of the general arguments over representative and direct democracy. Over the course of the past two hundred years America has gradually but surely moved towards increased democracy, which has occurred through an assortment of movements in advocacy of the rights of such disenfranchised populations as women and African Americans. Despite previous advancements of the government, scholars, citizens, and general observers alike remain unsettled by many aspects of the current political establishment. Polls frequently reflect that large majorities think the country is "on the wrong track," despite economic success (Haskell 3). Americans do believe they should be constantly looking over the shoulders of elected officials, and, whenever possible should wrest control from politicians and decide policy for themselves via initiatives, referenda, or other forms of direct democracy (Haskell 6).

Supportive of this notion is the popularity ballot initiatives to address a host of policy areas. While the legislative process is the most common mode of lawmaking, it is not the only one. The initiative process allows for the placement of a statutory or constitutional amendment on the ballot once proponents obtain a specified number of signatures while the referendum process involves laws passed by the legislature but on which the people must approve for enactment. Ballot initiatives have resulted in significant policy shifts in such areas as same-sex marriage, health care, euthanasia, land conservation, affirmative action, and tax and expenditure limitations. Initiatives have also changed fundamental aspects of the representative democracy system itself by bringing about legislative term limits and reforms for campaign financing. It has largely been by this process that the broad enactment of TELs, commonly referred to as the modern "tax revolt," has progressed.

Attentiveness to tax and expenditure limitations, including Colorado's TABOR Amendment, has recently been heightened due largely to two specific disparities among states. The first relates to long-term growth rates in state revenues and spending. Some states with TELs have limited the expansion of government better than states without, and questions on the role of TELs in limiting government expansion in those states have given rise to much recent literature. Second, responses among states to the revenue shortfalls that accompanied the national recession that began in 2001 differ significantly. Taxes were raised in some states, spending was reduced in others, and some accumulated substantial debt. Consequently, the overall influence of TELs on state responses to revenue shortfalls has become of particular interest to researchers (Poulson, "Tax and Spending" 1).

Also of interest are linkages between TELs and democracy since numerous TELs have originated via the citizen initiative process, and the exact function of most TELs is to mandate direct voter approval for various policy decisions, which invariably curtails the authority of elected officials. Just as the founders were passionate in their advocacy of direct and representative democracy, so too are current observers of the political system. Although the notion that ballot initiatives, such as tax and expenditure limitations, impact public policy is without question, the appropriateness of passing laws using this method is intensely disputed. The equivocal point of difficulty from which divergent views on democracy derive is how exactly citizens should participate in the political process?

Advocates of direct democracy contend that the allowance of initiatives and referenda is especially valuable since these measures provide a type of safety valve for the system of representative government in that they can compel policy changes when legislatures neglect policy areas. Although much literature by advocates of the initiative process acknowledges that moneyed special interests can, and sometimes do, undermine the integrity of the initiative process, much of it suggests that ultimately the process provides valuable opportunities for citizen and voter action, and it should remain so. Ernst, Larson, and Sabato summarize fundamental arguments by proponents of the initiative process and direct democracy who contend that such devices:

- Convey the popular will directly instead of it being diluted by representative politics and special interests;
- Reduce citizen alienation;
- Heighten voter awareness of issues; and
- Eliminate the corruption endemic to the legislative process (31-32).

Opponents of direct democracy provide a series of criticisms against, of which a central point is that initiatives and referenda constitute an unrefined means of legislating that yields ultimately piecemeal, poorly formulated law; this consideration is relevant to the current argument over constitutional reform in Colorado. For example, Colorado State Senator Abel Tapia, in a recent editorial, explained: “Through the years, amendments have tangled our constitution into an excessively detailed document with antiquated laws and conflicting provisions that straightjacket and cloud policy.

Unintended consequences have plagued the document by which we govern" (A3). According to a statement from the Colorado Municipal League, because it's just as easy to amend Colorado's constitution as it is to change state law through a ballot issue, the state constitution has become a crazy quilt of often conflicting mandates that together have unintended consequences (O'Brien).

Defenders of representative democracy also commonly raise two chief arguments in support of the representative democracy system. First, only representative institutions can fill the need for informed deliberation, consensus, and compromise, all of which are necessary for governance in the public interest. The campaign rhetoric used to pass referenda and initiatives is inferior to the consideration and compromise afforded by the representative democracy system.

Second, arguments for direct democracy presuppose that the opinion of the public has a special character and the majority by right should rule. Counter to this position is the notion that transforming the will of the majority into law can lead to the violation of minority rights by majority tyranny (Haskell 11). James Madison notably advocated representative democracy and the importance of institutional checks and balances as a means to protect minority interests. In Federalist No. 51 (Library), Madison explained:

> It is of great importance in a republic not only to guard the society against the oppression of its rulers, but to guard one part of the society against the injustice of the other part. Different interests necessarily exist in different classes of citizens. If a majority be united by a common interest, the rights of the minority will be insecure.

Ernst, Larson, and Sabato explain that the initiative process produces biases against individual and minority interests, which is exactly what representative institutions and the process of checks and balances were implemented to protect. And, simply put, legislatures and other representative government institutions promote certain democratic opportunities in ways that the initiative process doesn't, and they allow for a more thorough representation of mixed interests (42). Haskell asserts that the ability of minorities to use the legislative process to block popular legislation that they feel is threatening can be very frustrating at times. But liberal democracy is not meant to serve only the interests of the majority; it is meant to provide some protection for the rights of minorities as well. The alternative is a strict 50-percent-plus-one majoritarianism that runs the risk of leaving vulnerable minorities out in the cold. When contentious social issues come to the fore, plebiscitary politics can be a zero-sum game, and winning a majority may involve inflaming the public passions. The fact is that the values of consensus and compromise that are characteristic of representative institutions provide very real safeguards against this kind of politics (Haskell 159-60). Ernst, Larson, and Sabato summarize other common criticisms of direct democracy:

- Moneyed special interests dominate and adulterate the process;
- Voters lack an appropriate level of understanding of the measures on which they vote and the potential unintended consequences of those measures;
- Initiative constitutional amendments most seriously undermine the system of representative democracy since they are rigid in nature, may only be adjusted by another constitutional amendment, are not malleable by elected officials; and
- Initiatives and referendums can fix in place policies contrived by the uncertainties of shifting political coalitions (42).

Despite arguments for and against the use of direct democracy mechanisms, over seventy percent of Americans live in a city or state in which the initiative process is permitted, and use of the initiative process is widespread. In comparison to the $700 million spent on the closely contested 2004 presidential election campaign, nearly $400 million was spent on statewide initiative and referendum campaigns in the same year (Smith and Tolbert 1).

2.3 Early History of Tax and Expenditure Enactment

Prior to John Maynard Keynes' advocacy of government deficits and the importance of government spending to overcome the Great Depression, the prevailing, established set of attitudes favored government deficits only during times of war, and post-war surpluses were typically used to cover the debt incurred during war. The Keynesian revolution has plainly influenced the U.S. as well as other nations, and persistent deficits and a growing debt burden have been generally maintained. Over much of the post WWII period, the growth of state and local spending has outdistanced the growth of federal spending (Poulson, "Colorado's" 1). Frequently, following recessions states have raised taxes in order to compensate for revenue shortfalls, and when state economies recover, those higher taxes have tended to lead to higher state revenue collection and spending relative to state income.

The 1970s was a period marked by especially high inflation in California, and the method of raising taxes to overcome revenue shortfalls came to the forefront. While what is commonly alluded to as the modern "tax revolt" did not necessarily originate in California, the movement was greatly accelerated largely due to political activity in the state during the 1970s. On March 13, 1973, then-Governor Ronald Reagan offered Proposition 1 to the California state legislature, the first tax and spending limit submitted in state government. While Proposition 1 failed to pass, it popularized the concept of a tax and spending limit as a means to restrict government growth, and its provisions and structure have influenced subsequent limitations. Characteristics of Proposition 1 common to similar ensuing legislation include: limits on the growth of local and state government, an emergency reserve fund, the mandatory refund of surplus revenue, and required voter consent for tax increases.

Discontent over taxation persisted in California despite the failed passage of Proposition 1, and an assortment of citizen initiatives materialized, including Proposition 13 and Proposition 4, known as the Gann Amendment. Proposition 13, passed by California voters in 1978, sparked a national discussion that landed Howard Jarvis (the proposition's champion) a *Time* magazine cover and presaged similar successive legislation in other states. Within two years of the passage of Proposition 13, 43 states had implemented some kind of property tax limitation or relief, 15 lowered their income tax rates, and 10 indexed their income taxes for inflation (Mullins and Wallin 2-3). The Gann Amendment, which passed in 1979, also distinctly curbed prospects for the California state government. Since California's enactment of restrictive taxation measures, twenty-eight other states, including Colorado, have enacted tax and expenditure limitations, the attributes and effects of which are varied.

2.4 General Characteristics of Tax and Expenditure Limitations

The various types of state limitations can be categorized into three broad groups: revenue limits, expenditure limits, and hybrids. Revenue limits are those limits that link allowable state revenue retention to some measure, such as inflation or personal income. Expenditure limits link allowable annual state spending to growth indexes. Hybrids blend characteristics of both expenditure and revenue limitations.

Overall, Colorado's limitations are distinctive, as are those in each state. For example, some state TELs have minimal or even no impact on state budgeting, while the effects of others are much more binding. Limitations may differ based upon how they were enacted; whether they are statutory or constitutional; their degree of flexibility; how they handle the transfer of governmental programs; whether the TEL restricts spending or revenue; and how one TEL may interact with others enacted within the same state. Further, state TELs may also differ decidedly depending upon how the spending or revenue limit is calculated and the treatment of revenue collected in excess of the limit.

Despite the many characteristic differences of tax and expenditure limitations among states, there are certain fundamental attributes common to most TELS. It is largely diversity among these fundamental features common to most TELs that influences the specific nature of limitations in each state. It is also generally a combination of the features of TELs that affects their level of restrictiveness, and since the combinations of features vary across states, the restrictiveness of TELs on governments is also assorted among states.

Sources of Limits

How a TEL comes about can often affect how restrictive it is. TELs enacted by way of the citizen initiative process are usually more restrictive than those initiated by legislatures. Colorado's TELs have been enacted through both legislative and citizen action.

Revenue & Spending Limits

Since state officials generally possess more control over spending than revenue, revenue limits are conventionally more restrictive than spending limits. The state of

Colorado maintains both types of limits including TABOR, the Gallagher Amendment, Amendment 23, and the six percent limit.

Flexibility

The flexibility of TELs varies widely from state to state. For example, some TELs exempt specific categories of spending or revenues from their limits. Some common exemptions include Medicaid, debt service, federal mandates, and court orders. Also, some TELs allow for flexibility during economic recessions. Colorado's appropriations limit allows for greater flexibility than does its revenue limit.

Statutory & Constitutional Limits

Whether a limitation is constitutionally or statutorily enacted has significant implications since constitutional limitations are harder to change than statutory limitations. Changes to constitutional limitations require a referred measure, which voters may adopt or reject. Conversely, changes to statutory limitations, while politically risky, require a vote of the General Assembly and signature of the Governor, but not a popular electoral vote. While Colorado's revenue limit is constitutional, due to TABOR's provisions, voter approval is compulsory in order to weaken the provisions of the statutory appropriations limit.

Government Transfers & Limits

If governmental programs are transferred between federal, state, or local governments, several states permit a concurrent change to the limit. This is sometimes done to exempt certain programs from limits. Eighteen TELs don't have provisions addressing the transfer of responsibility of government programs (Legislative 22). Except for the area of K-12 education, Colorado's TABOR amendment enables local governments to reduce or end subsidies to any state mandated program.

Limit Calculation

There is also much variety among states regarding limit calculation methodologies. The most popular method of TEL limit calculation indexes government spending increases to the growth rate of state personal income (Legislative 22). Limits calculated this way are usually not as restrictive as those limits calculated by population growth or inflation since, over time, personal income generally grows more quickly than population growth and inflation.

Another method of calculating limits uses a fixed percentage increase above the prior year's appropriations. Limits of this nature are typically more restrictive, though exactly how much more restrictive they are depends largely on the size of the percentage increase. The revenue limit for the state of Colorado is computed using population growth and inflation, while the appropriations limit is computed simply by incorporating an annual, fixed percentage increase. Some studies suggest that those TEL limits based on population growth and inflation, like Colorado's TABOR limit, prevail as the most restrictive sort (Legislative 23).

Population Growth and Inflation	Personal Income	Percentage of Revenue Received	Percentage Increase Over Prior Year's Appropriations	Other[9]
Alaska	Arizona	Delaware	**Colorado**	California
Colorado	Florida	Iowa		Connecticut
Nevada	Hawaii	Mississippi		Massachusetts
Washington	Idaho	Oregon		Ohio
	Louisiana	Rhode Island		Oklahoma
	Michigan			Utah
	Missouri			
	Montana			
	New Jersey			
	North Carolina			
	Oregon			
	South Carolina			
	Tennessee			
	Texas			

Figure 1: Indicators Used to Calculate Tax and Expenditure Limits

Source: HJR 03-1033 Study: TABOR, Amendment 23, the Gallagher Amendment, and Other Fiscal Issues. Prepared by Colorado Legislative Council Staff, p. 23.

Handling of Surpluses

Surplus revenue is an amount collected in excess of a state's permissible revenue limit. States that mandate the refund of surplus revenue have more restrictive limitations than states that don't. Some states have limits so lofty that refunds are rarely made. In anticipation of future economic downturns, and in order to cope with such downturns, a number of states divert a portion of surplus revenue to rainy day funds. Colorado is one of ten states that require the immediate refund of surplus revenues to taxpayers. The requirement of an immediate refund is generally regarded as more restrictive because such a stipulation makes it difficult for states to retain any excess revenue for rainy day funds.

Ratchet-Down Effect

The limit for some states is based upon the lesser of the appropriations of the previous year or actual spending or revenue in the previous year. A state that uses this methodology will experience what is referred to as the ratchet-down effect, which occurs when revenue collected is below a state's allowable limit. When this occurs, the allowable limit for subsequent years is then reduced and it becomes quite difficult to increase that limit. Conversely, states that base limits on just the allowable limit of the previous year (not whatever was actual revenue or spending) avoid the ratchet-down effect. In Colorado, the ratchet-down effect was a problem during the recession, and voter approval of Referendum C eliminated the effect for future years.

Enforcement

Some state TELs specifically grant taxpayers the right to sue as recourse against the state should it fail to uphold the Amendment's requirements. Colorado's TABOR Amendment allows for such action by taxpayers to ensure that TABOR's provisions are adhered to. If plaintiffs are successful in such a lawsuit, TABOR requires that any revenue collected, kept, or spent illegally for four fiscal years prior to the filing of a suit is to be refunded with 10 percent simple, annual interest.

Summary

Much controversy surrounds direct democracy and the use of citizen initiatives to enact laws such as tax and expenditure limitations. Among the more prominent criticisms is the potential threat posed to minority interests when laws are made by sidestepping institutions and processes of the representative democracy system. The initiative process effectively allows the will of the majority to be transformed into laws that govern society as a whole, regardless of the impact of those laws on minority sub-populations. Colorado's TABOR amendment came about through the citizen initiative process, which makes questions concerning TABOR's impact on minority interests relevant. Due to its structure, characteristics, and placement in the Colorado Constitution, which makes voter approval mandatory for changes to it, Colorado's TABOR Amendment is widely deemed the most restrictive tax and expenditure limitation in the country.

3. Tax & Expenditure Limitations in Colorado

3.1 Overview

Written in 1876, the Colorado Constitution, which mandates a balanced budget and imposes restraints on practicable debt, is one of the longest and easiest to amend, a characteristic that explains the nearly 150 amendments to the constitution since its origination. As afforded by the Colorado Constitution, in practically every biennial election items are placed on the ballot to amend statutory law or the state constitution. Such items make their way on the ballot through the citizen initiative process or are referred to voters by the General Assembly. Regarding initiatives and referenda the Article V, section one of the Colorado Constitution specifies:

> The people reserve the right to themselves the power to propose laws and amendments to the Constitution and to enact or reject the same at the polls independent of the General Assembly and also reserve power at their own option to approve or reject at the polls any act or item, section, or part of any act of the General Assembly.

In comparison to other states, the public sector in Colorado is quite limited at the state level, and much authority is delegated to local governments. A 2004 report by Colorado Legislative Council Staff compared state and local government taxes in Colorado to those of other states. The report indicates the limited scope of state government in Colorado relative to other states. Sales and use taxes, individual income tax, and local property tax are the primary taxes paid by Colorado citizens. In 2004, Colorado ranked 49th nationally in state tax collections, while local governments ranked 7th nationally. Local governments rely heavily upon sales taxes and sales and use taxes for revenues, and most locally raised revenues for counties and school districts are derived from local property taxes.

Colorado citizens are commonly mistrustful of government. The Wells Fargo Public Opinion Research Program of the Graduate School of Public Affairs at the University of Colorado at Denver has surveyed registered voters in the state annually since 1994 and published the survey results in *Mind of Colorado*. Voters have been consistently questioned on their level of confidence in numerous Colorado institutions each year. Typically, the institutions in which most Coloradoans have the highest levels of confidence are the military, colleges and universities, charities and volunteer organizations, businesses, and local law enforcement. In 2003, the lowest ranked institutions were political parties (12 percent), organized labor (19 percent), Colorado state agencies (21 percent), and the state legislature (26 percent) (James and Wallis 20).

Colorado can be described as a leader nationally regarding the number of enterprises undertaken in an effort to restrain government spending and taxes. In addition to the enactment of TELs, the initiative process in the state has been used for a variety of issues such as term limits for elected offices. The mere threat of initiatives has frequently prompted legislators to act preemptively via statutes or by submitting a proposed amendment to voters—a response many other state legislatures have resorted to in the face of looming citizen initiatives (James and Wallis 21).

The first citizen initiative concerning the addition of a tax and expenditure limitation to the state Constitution was proposed in 1966. The 1966 initiative would have limited property taxes and made personal property taxes exempt from taxation. The 1966 initiative failed, as did others proposed in 1972, 1976, and 1978. Constitutional tax and expenditure limits and legislation relevant to such limits have since passed, which include the Gallagher Amendment, TABOR, Amendment 23, and Referendum C. The Arveschoug-Bird limit, also a prominent TEL, is a statutory limit.

3.2 The Arveschoug-Bird Limit

Passed in 1977, the Kadlecek Amendment imposed a limit on General Fund spending. The Amendment limited General Fund spending growth to seven percent above the prior year, mandated the preservation of a four percent reserve account, and provided that the excess revenues be used for property tax relief. The current General Fund appropriations limit, the Arveschoug-Bird limit[1] was enacted in 1991. The Arveschoug-Bird limit, named after Representative Arveschoug and Senator Bird who sponsored the bill that contained the limit, is more commonly known as the six percent limit.

The provisions of the six percent limit require that annual growth be limited to the lesser of five percent of Colorado personal income tax or six percent above total state General Fund appropriations in the prior fiscal year.[2] Legislators have generally interpreted the six percent limit as a floor since is advantageous to appropriate up to the appropriations limit in order to raise the appropriations base for the next fiscal year. Appropriating below the six percent limit serves to ratchet down the base for subsequent years.

The six percent limit does not apply to certain designated portions of the budget. Exceptions from the limit include: General Fund appropriations for property tax

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[1] C.R.S. §24-75-201 (1).

[2] C.R.S. §24-75-201 (1) (a) (II).

reappraisals, revenues derived from a voter-approved increase in the rate or amount of any new tax or fee, new federally mandated programs, or supplemental appropriations for Medicaid. Additional areas of the budget excluded from the 6 percent limit include General Fund transfers to the Capital Construction Fund[3] and the Controlled Maintenance Trust Fund[4].

3.3 The Gallagher Amendment

In 1982, national concern over property taxes was pronounced. The Colorado Legislature proposed the Gallagher Amendment to voters to prevent a tax revolt in Colorado similar to California's, and the measure passed. The Gallagher Amendment[5] is a constitutional amendment with two functions. First, the amendment reduced the percentage of local property taxes paid by owners of residential property, and second, it froze that percentage in place.

Property taxes are determined by multiplying two variables: the taxable value of property (assessed value) by the local tax rate (mill levy). Assessed value is determined by multiplying the property value by an assessment rate. The amendment requires adjustments of the residential assessment rate yearly so that the percentage of assessed value attributable to residential property remains the same from year to year. The overall effect of the Gallagher Amendment is to keep residential property taxes down, even as home values rise. Colorado's economic boom during the 1990s resulted in a sharp rise in

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[3] C.R.S. §24-75-302 (2): Excludes General Fund transfers to the Capital Construction Fund from the six percent limit.

[4] C.R.S. §24-75-201.1 (1) (c.5) (II): Excludes transfers to the Controlled Maintenance Trust Fund from the six percent limit.

[5] *Colorado Constitution*, Article X, Section (3) (1) (b).

residential property values. However, in accordance with the provisions of Gallagher, this growth was exempt from taxation.

Seventeen other states use different assessment rates to reduce the residential property tax burden. Some offer credits or exemptions, while others maintain limits on increases in property taxes for individual properties. The Gallagher Amendment uniquely curtails the percentage of property taxes paid by all owners of residential property statewide, irrespective of individual properties.

3.4 The Taxpayer Bill of Rights (TABOR)

3.4.1 National Context in Which TABOR Was Approved

Tax and expenditure limitations were again popularized throughout the early 1990s, and ten new TELs were enacted between 1990 and 2005. The TELs enacted in the 1990s differed from those passed in the first wave in that the emphasis of the TELs passed in the second wave was limiting state spending and government growth rather than reducing the existing tax burden (Hill et al. 18). To this end, those TELs passed in the second wave limited revenue collection or spending to indexes like population growth or personal income growth.

There are assorted opinions concerning causes underlying the rise of TEL enactment in the 1990s. Mullins and Poulson point to the recession of the early 1990s as a motivator for renewed interest in TELs. Poulson attributes the rise to differences in the long-term growth rates in state revenues and the growth rates of state spending, and to the varying government responses to recessionary revenue shortfalls among states in the 1990s (Poulson, “The Next”). Mullins asserts that voters in states without TELs became increasingly frustrated with the proportion of government spending relative to the overall economy (Mullins and Wallin 113).

New, Stansel, Johnson and McKacken emphasize voter participation in the 1990s, and indicate that direct democracy and voter dissatisfaction were heightened during this period. New asserts that direct democracy was gaining popularity during the 1990s, evidenced by the 1996 election in which American voters encountered over 90 statewide initiatives and nearly 200 local initiatives or referenda (4). Stansel refers to the increased enactment of TELs in the 1990s as a broad-based political movement, and points out that between 1992 and 1994, five states passed TELs (Stansel 91). Johnson and McKacken concur, and suggest that the American electorate in 1992 and 1994 was swelling with anti-tax, anti-government sentiments.

3.4.2 History of TABOR's Enactment

Colorado was no exception to widespread anti-tax sentiments, and after three prior failed attempts, in 1992 Colorado voters endorsed the Taxpayer Bill of Rights. Like California's Proposition 13, TABOR's passage was also the result of citizen initiative. In 1986, Douglas Bruce, a Colorado Springs resident, began his crusade for TABOR and it was ultimately placed on the ballot for voter consideration. The intent of the proposed amendment was to require voter consent for new taxes or tax increases, which would invariably reduce the scope of influence of Colorado state and local government officials. Despite incipient, broad support among voters, the amendment failed. This was to be the Bruce's first of four initiatives proposed to markedly curtail the adequacy of the Colorado government.

In 1988, Douglas Bruce insistently advocated for a second, more demanding initiative that would have required voter approval for new state or local tax increases; reduced state income taxes by ten percent; limited local residential property taxes to one percent; and, unless approved by voters, would have overturned state and local tax increases passed between 1986 and 1988 (James and Wallis 22). As in 1986, support for the amendment was high at the outset, but then diminished subsequently in the face of a well-funded, well-organized opposition campaign. According to *Denver Post/ News 4* polls, support for the amendment on October 5, 1988 was 60 percent, but dropped to 45 percent on October 27, just twenty-two days later (James and Wallis 22). Constituents of the opposition to Bruce's amendment included: U.S. West (which has since become Qwest), Adolph Coors Co., the Colorado Cattleman's Association, then Colorado's Governor Roy Romer, various education groups, and numerous prominent executives and political leaders. Ultimately, Bruce's second attempt also fell short.

Bruce was not dissuaded by the second defeat, and in 1990 mounted an attempt in advocacy of a third initiative. This initiative offered a limit on the growth of state spending, required voter approval for tax increases, and a limit on local property taxes. Support for this initiative surpassed that of the previous two, and prominent state leaders stood by it as well. Moreover, the campaign for the third initiative raised more capital, which was particularly advantageous as it allowed Bruce to buy television time. Despite heightened support, the third initiative received only 48.9 percent of votes and thus failed by 21,600 votes (James and Wallis 23).

In 1992, Douglas Bruce finally triumphed with his fourth and final initiative, now known as the TABOR Amendment, which passed with 53.7 percent of votes in favor, 46.3 percent of votes against (James and Wallis 23). When TABOR passed in 1992, Colorado was already one of the most fiscally conservative states. According to a statewide Colorado Citizens Poll conducted in 1992, 63 percent of participants proclaimed that state and local taxes were too high and that government should address the issue (James and Wallis 23). Well-organized backing from Conservatives and business groups decidedly promoted Bruce's fourth attempt. Concisely, the message conveyed to voters was that lower taxes would improve the economy—a message similar to that used to promote California's Gann Amendment—and polling data suggests that this message was aligned with the majority of voter sentiments.

Another factor contributing to TABOR's passage was decreased opposition to the Amendment. Instead of TABOR, an amendment aimed at K-12 education was Governor Romer's central focus during the 1992 election. Also, apart from the outright rejection of TABOR, the Colorado legislature failed to provide voters with an option other than Douglas Bruce's proposed TEL.

3.4.3 Main Provisions of TABOR

TABOR is the state's most confining limit and, from special library districts to the state level, it applies to every level of the Colorado government. Over 1900 words long, the TABOR amendment governs practically every state revenue and expenditure decision made in the state of Colorado ("The Colorado Budget"). The general provision of TABOR states, "It's preferred interpretation shall reasonably restrain most of the growth of government."[6] TABOR was proposed as a measure to: slow taxes and spending growth at the state and local government levels; control and provide information about local debt; put the people more in control of their taxes; encourage

[6] *Colorado Constitution*, Article X, Section (20).

better utilization of public monies; create incentives for fiscal prudence and government productivity; and ultimately stimulate business and job growth (Holden).

The TABOR amendment has four central provisions that function to: require voter approval for government revenue increases, limit revenue growth, freeze existing spending limits, and limit taxation options.

(1) Voter Approval for Revenue Increases

TABOR requires that voters agree to any new tax, increase of tax rates, mill levy increases, or the extension of an expiring tax or a tax policy change directly causing a net tax revenue gain for the government. TABOR does allow for decreases of tax rates, mill levies, and debt limits without the requirement of voter consent.

(2) Revenue Growth Limit

Principally, the purpose of TABOR revenue limits is to prevent annual allowable state revenue collections from exceeding inflation plus population growth. If collected revenue does exceed TABOR's limits, then that quantity collected above the limits must be refunded to taxpayers. The first two refunds made to Colorado taxpayers took the form of a sales tax refund. There are now a total of 19 separate refund mechanisms. Voters may also choose to forgo refunds or tax cuts, and approve measures that allow the government to maintain possession of the excess collected revenue.

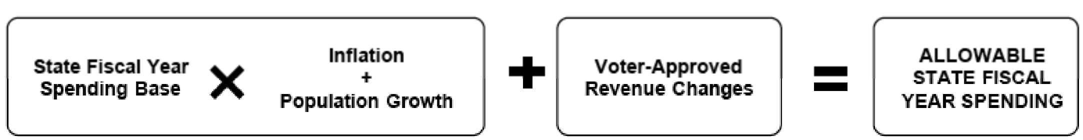

Figure 2: Formula for Calculating the TABOR Limit Imposed on the Colorado State Budget, Article X, Section 20 (7) (a) of the Colorado Constitution.

Source: Colorado Legislative Council, "State Limits on Appropriations and Spending," December 2004.

Figure 2 shows the formula used to calculate *all* allowable state fiscal year spending. At the state level, population change and inflation are integral fragments of limit calculation. Growth for most state revenue is limited to the Denver-Boulder-Greeley inflation rate, which takes into account the change in various prices of products bought by consumers in the three cities, plus the annual percentage change in the state's population.[7] Throughout the 1990s, the population of Colorado grew at an average of 2.3% annually—the third highest growth rate in the nation—and between 1992 and 2002, Colorado's population exceeded 4.4 million (Hedges et al.). TABOR proponents suggest that the combination of population growth and the CPI provides a measure of the growth of the state economy, and, as such, provides the measure of comparison for which the appropriate level of retained government revenue should be based.

For TABOR limit calculation at the local level, the inflation rate remains, but other criteria are incorporated in the allowable revenue growth formulas. Figure 3 indicates the various TABOR formulas. While the Denver-Boulder-Greeley CPI figure is the same in calculating TABOR formulas for allowable growth in government spending, the growth factor for local governments is net new construction, and the growth factor for school districts is change in enrollment.

[7] C.R.S. §24-77-103 (2): Specifies the procedures for calculating state population growth for the TABOR revenue formula.

State	Local	School Districts
CPI + % Change in Population	CPI + % Change in Net New Construction	CPI + % Change in Enrollment

CPI, Denver-Boulder-Greeley Consumer Price Index.

Figure 3: TABOR Formulas for Calculating Allowable Growth in Government Spending.

Source: The Bell Policy Center, *Ten Years of TABOR: A Study of Colorado's Taxpayer's Bill of Rights* (Denver: The Bell Policy Center, February 2003).

(3) Voter Approval and Existing Limits

TABOR's "weakening provision" ensures that existing revenue limits, spending, and debt can only be weakened by voter approval, which means that when TABOR passed, the weakening provision fixed into place all other limitations. Officials may lower those limitations at any time, but raising the limitations requires voter approval. While the government may spend less than the statutory limits allow, revenue that is not spent in one year can't be used during the next year.

(4) Restrictions of Taxation Options

TABOR also encumbers taxation options for state and local governments. Tax districts must receive voter permission for new taxes, a local mill levy increase extending a tax set to expire, or tax policy that leads to a net tax revenue gain. A state income tax change must have a single rate, and income tax increases must take effect a year after they are approved. TABOR disallows altogether the imposition of certain types of taxes including: new or increased real estate transfer taxes, state real property tax or local district income tax, or new surcharges on state income taxes.

3.4.4 TABOR Surplus Refund Mechanisms

When revenues collected exceed the allowance afforded by the TABOR formula, excess collected revenues, per TABOR, are to be refunded to taxpayers. However, the exact processes by which refunds are to be made is not clearly specified within the TABOR law. The absence of clarity in this matter has led some to question how refunds in Colorado have been allocated. More specifically, some critics (e.g. Poulson) argue that vagueness regarding the distribution of surplus expenditures has allowed legislators to pursue a political agenda benefiting interest groups—without voter approval.

Although TABOR passed in 1992, revenues were below the TABOR revenue limit until 1997. When legislators realized that funds would have to be refunded, their response was to seek voter approval to forgo the refund. But voters declined. Regardless, legislators have persistently increased spending growth over the amount allowed by TABOR because of the past accumulation of reserve funds (Surplus 12). According to Poulson, in recent years the Legislature has chosen to offset surplus revenues with tax refunds and tax cuts that have very little to do with the generation of the surplus revenues. This has permitted legislators to pursue a political agenda benefiting a variety of different interest groups (Surplus 12).

Poulson also notes, "The TABOR Amendment has had a perverse outcome for budgetary decision making…The TABOR Amendment has resulted in budgetary decisions that are less efficient and less equitable than those that would have been made in the absence of the surplus revenue" (Surplus 12). TABOR was not passed to provide legislators with the ability to provide tax refunds and tax relief to specific interest groups, and this aspect of TABOR represents an unintended consequence.

3.5 Amendment 23

In FY 1999-00, the state of Colorado ranked 46th in the percent of expenditure on schooling (James and Wallis 16). The TABOR formula was in effect, but school expenses surpassed inflation and spending per pupil decreased consequently. To address disparities between Colorado and other states in the area of public school funding, teacher unions proposed Amendment 23, a November 2000 ballot initiative. At the polls, fifty-four percent of voters approved the amendment (James and Wallis 24).

Like TABOR, Amendment 23 is a highly controversial constitutional measure that has considerably impacted state revenue allocation since its enactment. The amendment passed in 2000 at the end of an economic boom that had resulted in significant surplus revenues. In promoting Amendment 23 to voters, some advocates even indicated that surpluses would persist and that those revenues would be available to fund the requirements of the amendment, which was not the case in 2001.

Amendment 23 made four significant changes to state funding for K-12 public education. Overall, the four main provisions of Amendment 23 ensure funding increases for K-12 public education funding.

(1) Statewide Base Increases in the School Finance Act

The Amendment requires that the statewide base in the school finance act increase by a minimum of inflation plus one percent through FY 2010-11, and by the rate of inflation thereafter. The statewide base is the per-pupil funding amount for districts, which varies among districts due to such factors as a school district's size and living costs.

(2) Categorical Program Funding Increases

Amendment 23 requires that total funding for all categorical programs be increased by at least inflation plus one percent for ten years. Funding for all categorical programs is to increase by the inflation rate after that. Categorical programs are intended to serve specific groups of students or student needs, such as English language proficiency programs, special education programs, and expelled and at-risk student programs. The General Assembly allocates the total funding increase among categorical programs as it sees fit.

(3) State Education Fund

Amendment 23 establishes the State Education Fund (SEF) and transfers one-third of one percent of federal taxable income to the Fund. Revenues transferred to the Fund are exempted from both the TABOR limit and spending of Fund revenues exempted from the six percent appropriations limit. SEF revenue can be used for a variety of uses such as class size reduction, public school building capital construction, improving student safety, and compliance with the requirement to increase categorical program funding annually.

(4) Maintenance of Effort

The maintenance of effort provision is an especially significant component of Amendment 23 that functions to guarantee funding increases to K-12 public education. The provision requires General Fund contribution increases to the school finance act by a minimum of five percent every year through FY 2010-11 if personal income grows by at least four and one-half percent.

Summary

Colorado has historically maintained stronger local governments relative to the state government, and Coloradoans have traditionally preferred that government maintain a smaller role. Colorado can be described as a leader nationally regarding its limitations enacted to restrain government growth. Colorado maintains the six percent limit, the Gallagher Amendment, TABOR, and Amendment 23, and each limitation affects specific areas of the budget.

In short, the six percent limit applies to the state's General Fund, and limits appropriations to six percent above the prior year's total state General Fund appropriations. The Gallagher Amendment limits the amount of revenue that can be collected from residential property owners. Voters approved TABOR as a means to limit the growth of government. TABOR limits total state revenue collection to inflation plus population growth, requires voter approval for certain state actions, and limits taxation options. Amendment 23 requires annual increases for K-12 education funding.

4. The Colorado Economy & Government Revenues

4.1 The State Budget Process

Colorado's TELs serve to guide the budgeting process in that they collectively influence options for state revenue retention, spending, and allocation. The process of establishing the state budget in a given year is a lengthy process, lasting around a year from beginning to end, and is one in which the influence of TELs is especially well known to budget officials.

The Joint Budget Committee (JBC), the six member committee that dominates the Colorado state budget, is comprised of the Chairman of the House Appropriations Committee, one House majority party member, one House minority party member, the Chairman of the Senate Appropriations Committee, one Senate majority party member, and one Senate minority party member.[8] The JBC and its staff of sixteen prepare the state budget throughout the year, and then submit the "Long Bill" to the legislature for its approval and ultimately the Governor's signature.

While it is within the scope of the legislature's duties to write and pass the budget, the Governor's office is significant to the process. The fiscal year begins July 1, and ends June 30, but the legislative and executive branches coordinate throughout the entire year as the state's budget needs fluctuate. The governor's office oversees the operation of state government departments, and each year is responsible for creating an

[8] C.R.S. §2-3-201 (1).

executive budget that outlines funding priorities, revenues, and expenditures. The executive budget is then submitted to the JBC.

Once the JBC receives the executive budget, the JBC holds hearings with the various departments. Each of the sixteen members of the JBC staff is assigned to a specific department. The staff members carefully review the executive budget request, meet with representatives from departments, and then present relevant information to the JBC in November. Following JBC staff briefings, the JBC begins hearings with the departments. JBC hearings allow JBC members to further assess departmental budget requests by asking departmental staff about new funding needs and general issues concerning the department's fiscal status in the next fiscal year.

Actual preparation of the Long Bill begins at the end of January. The General Assembly is responsible for specifying how much revenue will be available for appropriation in the next fiscal year, which is asserted in a joint resolution. In order to establish the revenue figure, the General Assembly can review revenue projections prepared by the Governor's Office of State Planning and Budgeting and those forecasts made by the General Assembly's economic office. The amount of revenue available for appropriation is highly important since the Colorado constitution mandates a balanced budget each year, and the dollar amount specified by the General Assembly is basis for determining whether the budget is balanced. Appropriated funds cannot exceed the total available funds for appropriation.

Throughout February and March the JBC and staff comb through department budget requests, compare requests with funds available for appropriation, and the JBC votes on each line item. JBC staff prepares and balances the Long Bill, and it is sent to both houses of the General Assembly where it is routed through the same legislative process that every other bills is. Each party holds a caucus to discuss the Long Bill, question JBC staff, and formulate amendments to be offered to the bill during second reading. The Long Bill passes to the floor where its merits are debated by the House and Senate. Once it passes both houses, it is sent to the JBC, which serves as the conference committee that reconciles any differences between the chambers. The JBC conference committee report is sent to both houses for adoption.

The Governor receives the Long Bill after it has passed both houses, and is authorized only to veto particular line items in the bill. The Long Bill finally becomes law once the Governor signs it, and responsibility for administering the budget throughout the year is within the scope of the duties of the Governor's Office.[9]

The structure of the state budget can change throughout the year as economic conditions and the budget needs of departments fluctuate over the course of a fiscal year. Departments are able to make supplemental funding requests, which are supposed to be submitted by the Office of State Planning and Budgeting to the JBC by January 1, but later requests can be submitted to address unusual or unforeseen circumstances.[10] The JBC reviews supplemental requests and determines whether the request should be met with additional funds and the source of those funds. The balanced budget mandate outlined in the constitution implies that for supplemental requests to be granted to a particular department, budget cuts must be made somewhere. The General Assembly ultimately votes on supplemental appropriations bills.

[9] C.R.S. §24-37-301 (1).

[10] C.R.S. §24-37-304 (1) (b.5).

4.2 Categories of State Funds

The state receives revenues from a number of sources including federal grants, taxes, fees and fines. Once collected, revenue is allocated among various state funds for the payment of state government operations. A host of restrictions affect how much revenue can even be in each type of fund and how legislators may spend the money in each fund. State revenues are divided into four categories: (1) General Funds, (2) Cash Funds, (3) Cash Funds Exempt, and (4) Federal Funds.

Of the primary categories of state funds, the uses of three are fairly rigidly defined, which makes General Funds especially significant to the state budgeting process. Reliance upon the General Fund varies among agencies. Some agencies, like the Department of Corrections, depend on the General Fund almost absolutely. Numerous agencies receive revenues from a combination of fund types. For example, the Department of Higher Education receives General Funds and raises revenue through tuition and student fees. Other programs and departments, like the Department of Regulatory Agencies, receive revenues nearly entirely from Cash Funds.

(1) General Funds

Of the state funds, the General Fund is the largest and most flexible, and is used predominately to facilitate the main functions of state government. General Funds are the least restrictive and most competitive funds, and legislative debate on the budget is most often debate over the use of General Funds. The General Fund is also the fund from which TABOR refunds are made. The source of General Funds is state tax revenues, such as sales and income taxes.

(2) Cash Funds

Cash Funds come from taxes, fines, and fees and are designated for the specific programs or purposes for which they are collected. Examples include transportation fees and tuition for higher education.

(3) Cash Funds Exempt

Cash Funds Exempt are cash funds exempted from TABOR restrictions. Examples of Cash Funds Exempt are funds transferred between government agencies and donations to the state. Revenues raised from enterprises such as the State Fair also qualify as Cash Funds Exempt. The remainder of Amendment 35 taxes (cigarette taxes) is counted as Cash Funds Exempt too.

(4) Federal Funds

Federal Funds are those received from the federal government. These funds may be designated for short-term use or long-term, joint federal-state programs such as Medicaid. Matching state funds may also be a requisite for receipt of Federal Funds.

4.3 The Spending of State Revenues

In addition to Colorado's TELs, state budget decisions are influenced by an assortment of other limitations that affect how state revenues are spent. Federal Funds are usually accompanied by spending requirements, and the executive branch has discretion over spending for most Federal Funds. Cash Funds and Cash Funds Exempt are designated for specific programs and uses. In short, the uses of three of the state's four categories of funds are fairly rigidly defined. Since the General Fund is the least restricted fund, it is central to the budgeting process. But there are limitations on General

Fund use too. Over 90 cents of every General Fund dollar is spent on six categories of essential services, which leaves very little available for other programs and services.

Underlying cost drivers and laws that require minimum funding levels influence the funding structures for the six main programs. For example, state and federal laws require the provision of at least a basic education system for every child, minimum benefits through the Medicaid program, and mandatory sentencing laws that correspond with prison population growth and higher corrections spending.

The budget needs of programs also expand with rising operational costs, such as medical services and training for personnel ("The Colorado Budget"). The overall influence of state and federal laws and underlying cost drivers on legislators is significant because they limit the ability of legislators to set and fund other priorities. Legislators in all states face somewhat similar encumbrances with respect to federal and state law compliance and cost drivers. However, the situation in Colorado is made considerably more complicated because of Colorado's tax and expenditure limitations and their varied requirements.

Summary

The implications of the budget's composition in each fiscal year are vast. Around the state, the budget affects local economies, living conditions, and various sectors such as public health, education, and corrections. Forming the state budget is a complicated process that is made more complex by Colorado's tax and expenditure limitations. TABOR limits total revenues legislators have to work with, and the six percent limit caps General Fund spending. Amendment 23 mandates K-12 education funding increases, and Gallagher holds down property tax revenues. Further, underlying cost drivers also influence the state's budget needs and can affect the allocation of funds across departments.

Legislators have limited options and maneuverability when it comes to budget decisions. The General Fund is key to most state operations and programs since the uses of General Funds are the least restricted. But General Funds are also burdened by restrictions since over 90 cents of every dollar is spent on the provision of essential services. Cash funds are for designated uses, typically for the programs or purposes for which they are collected. Cash Funds Exempt are exempt from TABOR restrictions and represent a very small portion of the budget. Federal Funds often involve specific requirements for their use, such as the provision of certain programs or services to certain populations.

5. The 2001-04 Recession

5.1 Colorado Economy During the Recession

The Colorado economy prospered throughout the 1990s, and by many standards Colorado's economy even outdistanced that of the nation. From 1991 to 2000, Colorado employment increased yearly at a rate of 4.1 percent and over 670,000 jobs were created; national employment increased annually by 2.2 percent during the same years (Legislative 3). The Colorado population increased at the third fastest rate nationally between 1990 and 2000 as it rose by over one million, and personal income increased annually at a rate of 8.2 percent throughout the decade, the second fastest rate nationally (Legislative 3).

Three sectors of the Colorado economy drove the upswing: advanced technology, construction, and tourism. Within the advanced technology sector it was the telecommunications industry that grew especially. Employment and the average wage in the Colorado telecommunications industry doubled during the 1990s, and the industry invested considerably in fiber-optic cable networks. Further notable growth in the advanced technology sector included the software and advanced technology manufacture industries as national investment in these products surged. To meet the demands of Colorado's expanding population, the advanced technology and telecommunications firms invested in commercial real estate, and residential construction swelled to meet rising demands of the expanding upwardly mobile population. Finally, the strength of the national economy promoted the tourism industry as households prospered.

As the national economy slid into recession in 2001 so did Colorado's. It was the sectors that drove the boom during the 1990s that suffered the most during the recession. The advanced technology boom ended in March 2000. The telecommunications industry suffered from a mismatch of supply and demand (cable was in oversupply while demand worldwide diminished). Residential and commercial construction declined. And the events of September 11 adversely impacted the tourism and airline industries. Also compounding the recession in Colorado were wildfires that further damaged the tourism industry and an acute drought in the summer of 2002 that reduced crop harvests.

Colorado lost over 81,000 jobs between December 2000 and July 2003. Personal income growth fell from 11.4 percent in 2000 to 3.6 percent in 2001, and then to 0.8 percent in 2002. Nonresidential construction fell 14.2 percent in 2000, 0.6 percent in 2001, and 20.9 percent in 2002 (Legislative 4). Colorado's recession was worse relative to that of the nation since Colorado's economy had been bolstered by the three sectors hardest hit nationally—advanced technology, telecommunications, and tourism.

	Total Personal Income		Employment		Population	
Year	**Growth**	**Rank**	**Growth**	**Rank**	**Growth**	**Rank**
1995	8.3%	3	4.5%	4	2.8%	4
1996	7.6%	9	3.6%	6	2.4%	4
1997	8.8%	3	4.2%	4	2.5%	3
1998	8.9%	5	3.9%	3	2.4%	3
1999	8.4%	1	3.6%	3	2.7%	3
2000	11.4%	2	3.8%	3	2.4%	3
2001	**3.6%**	**26**	**0.6%**	**17**	**2.4%**	**3**
2002	**0.8%**	**49**	**-1.9%**	**49**	**1.7%**	**6**

Figure 4: Colorado Economic Indicators 1995-2001 and National Rankings.

Source: Bureau of Economic Analysis, Bureau of Labor Statistics, U.S. Census Bureau.

Figure four indicates Colorado's ranking nationally in the areas of total personal income growth, employment growth, and population growth from 1995-2002. Colorado lost more income and jobs than most states, and the state ranked 49th in both categories in 2002. The economic downturn and significant job losses placed a heavy burden on Colorado's state government, and the compelling restrictiveness of Colorado's TELs became widely known.

Throughout the expansion of the 1990s, General Fund expenditures were limited by Colorado's constitutional and statutory limits. Surpluses were refunded to taxpayers, the six percent limit constrained General Fund appropriations, and, due to Colorado's prosperity, a fairly significant volume of highway and capital construction could be funded. The recession changed Colorado's budget situation drastically since the status of the economy corresponds with revenues collected by the state.

The recession reduced revenue collections to such a degree that falling revenues became the new constraint for legislators. Both income and excise taxes contributed to over 90 percent of General Fund revenue from FY 1990-91 through FY 2002-03, which is significant because the collection of these taxes is highly sensitive to economic conditions. Between FY 2000-01 and FY 2002-03, revenues from income taxes decreased by $1 billion, and revenues from excise taxes decreased by $89.1 million. In order to supplement General Fund revenues during this period, the General Assembly transferred cash funds to the General Fund, a course of action not taken since FY 1991-92, also a time of financial difficulty for the state when $11.6 million in transfers from the Capital Construction Fund had been transferred to the General Fund.

Individual income tax revenue is highly correlated with salaries and wages. In FY 2001-02, personal income growth was stagnant in Colorado, and employment declined. Capital gains are also relevant to individual income tax revenue and can be unpredictable. Throughout the 1990s, capital gains contributed to double-digit income tax growth. Conversely, capital gains contributed to significant declines from 2001 through 2003. Capital gains contracted 44.5 percent nationally in 2001.

Corporate profits fluctuate in an unpredictable fashion, as do corporate income taxes. Between FY 1990-01 and FY 2000-01, corporate income taxes increased annually by 11.1 percent, but declined 46 percent in FY 2001-02. The decline was largely due to the national recession and its repercussions for corporate earnings, especially for the telecommunications and advanced technology sectors, and the events of September 11 2001. Corporate income taxes did increase 26.4 percent in FY 2002-03, but were still $104.6 million less in FY 2002-03 than they had been in FY 2000-01.

From FY 1990-91 through FY 2000-01, sales and use tax increased annually by 8.5 percent, and during this same period, personal income increased yearly at 8.2 percent. In FY 2001-02, personal income growth was 0.3 percent, but sales and use taxes decreased 2.2 percent. Sales and use taxes decreased 3 percent further in the next fiscal year.

5.2 Legislative Responses to the Recession

Throughout the 1990s, the economic upswing positively affected General Fund revenues, which were constrained by Colorado's limits on revenue collections and spending. Total General Fund expenditures increased yearly by 7.8 percent between FY 1989-90 and FY 2000-01 from $2.6 billion to $5.94 billion. The situation changed dramatically in 2001 when declined collected revenues forced General Fund spending reductions. In FY 2001-02 General Fund spending decreased by $221 million and by $96 million in FY 2002-03 (Legislative 7). General Fund spending finally increased by $82 million in FY 2003-04.

In response to declined General Fund revenues, legislators employed three strategies. First, constitutionally protected programs and those relevant to public health and safety were made a priority. Once prioritized, those programs low on the list and unable to be funded easily via other means were either scaled back or terminated altogether. Second, legislators scoured for programs for which funding could be reduced or supplemented with revenues from sources other than the General Fund, and raised fees and fines for such programs. Third, General Fund revenues were supplemented with revenue from Cash Funds in order to at least preserve the state's core services.

5.2.1 Prioritization of Government Programs

During the recession, not only did the level of General Fund expenditures fall during the recession, but also the distribution of General Fund spending changed (Legislative 7). Programs categorized as necessary for public health and safety and constitutionally mandated programs were made a priority. The Departments of Education, Health Care Policy and Financing, and Corrections all received greater funding from the General Fund. General Fund spending for the six largest departments increased from $5 billion to $5.3 billion between FY 2000-01 and FY 2003-04. General Fund spending for education increased by 12.8 percent between FY 2001-02 and FY 2003-04, much of which was due to mandated funding increases in accordance with Amendment 23.

During this period, total General Fund spending for education increased overall from 37.3 percent to 42.4 percent of the General Fund.

State budgeting in Colorado is a zero sum endeavor, so increased support for the major departments invariably corresponded with decreased funding elsewhere. The percentage of General Funds allocated to the six major departments was 93 percent in FY 2003-04, which constituted the highest percentage in the preceding fifteen years. Spending on other departments was cut by $82.3 million between FY 2000-01 and FY 2003-04, and capital construction spending was reduced by $276 million (97 percent). General Fund spending for the Department of Higher Education decreased by $156 million and funding for the Department of Human Services decreased by $30 million. Figure five indicates how General Fund spending was allocated among departments from FY 2000-01 to FY 2003-04.

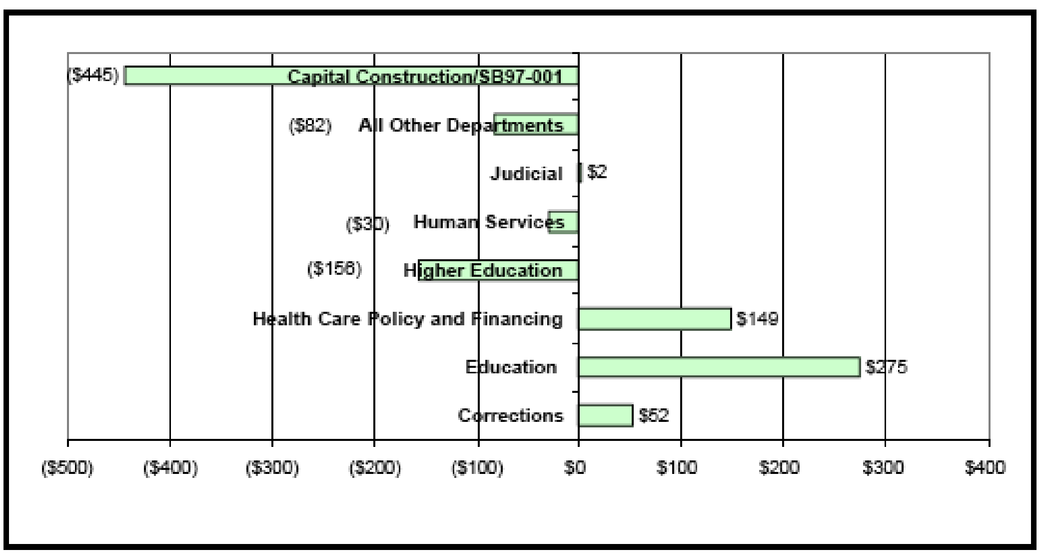

Figure 5: Change in General Fund Spending (in millions of dollars) between FY 2000-01 and FY 2003-04.

Source: Colorado Legislative Council Staff, p. 12.

5.2.2 Changes to State Program Funding Mechanisms

Despite decreased General Fund allocations to many programs, several of those programs still experienced overall funding gains during the recession because of their funding structures. Due to the shortage of General Funds, officials identified programs for which revenue sources other than the General Fund were available to fund the operations of departments. While those programs received fewer General Fund dollars, numerous existing fees and fines were increased and others were instituted. An example of this scenario is Senate Bill 03-261. In order to address the absence of General Funds, Senate Bill 03-261 both raised existing fees and imposed new fees to fund the Division of Property Taxation, a division in the Department of Local Affairs.

Officials also instituted fees that would enable the state to receive matching federal funds. For example, Senate Bill 03-266 created a new daily per patient fee imposed on selected nursing homes. The fee imposition allowed for reduced General Fund allocations to the nursing facilities, matching federal Medicaid funds, and reimbursement for Medicaid services.

5.2.3 Use of Cash Funds and Other Revenues to Supplement the General Fund

Finally, revenues from Cash Funds were transferred to the General Fund in order to facilitate increased spending for The Departments of Education, Health Care Policy and Financing, and Corrections. Transfers to the General Fund were substantial. In FY

2001-02, net transfers from Cash Funds totaled $1 billion. In FY 2002-03, net transfers totaled $206.2 million (Legislative 13).

5.3 Legislative Council's Assessment of Colorado's TELs and the Recession

In September 2003, Legislative Council Staff, the General Assembly's own research department, assessed the interaction of TABOR, Amendment 23, and the Gallagher Amendment to provide the General Assembly with an understanding of how the TELs impacted the state's ability to cope with the recession. The report provided several options for addressing the difficulties imposed by Colorado's TELs and making the state TABOR limits more responsive to the economy.

5.3.1 Revenue and Spending Limits

Actual revenues in FY 2001-02 became the TABOR base for calculating the next year's limit and were $356.7 million below the TABOR limit for FY 2001-02. Revenue in FY 2002-03 was $703.6 million below the TABOR limit for that year. TABOR's ratchet-down effect made the declined revenue bases permanent, and thus lowered the quantity of revenues the state could keep. Figure six outlines the differences between the TABOR limit without the ratchet effect, which began in FY 2001-02, and the actual TABOR limit based on declined revenues. As a consequence, state legislators had even fewer dollars to allocate during the recession.

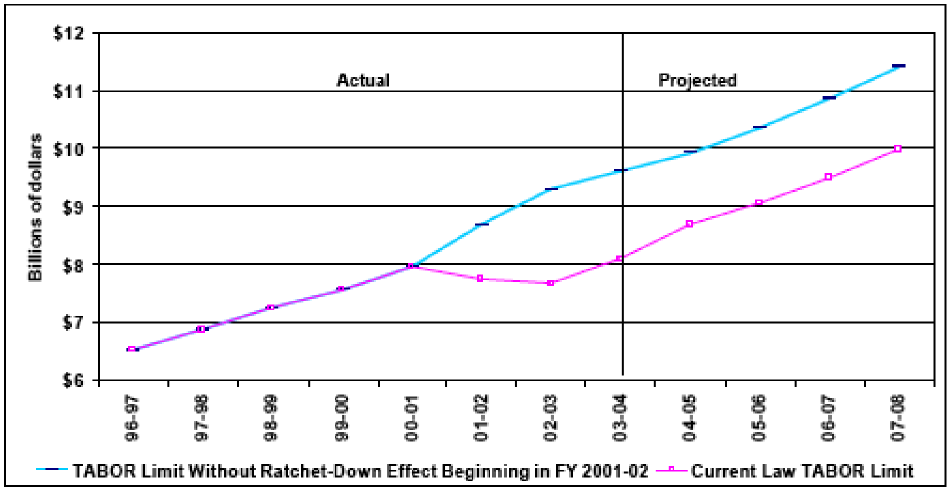

Figure 6: The Ratchet-down Effect and Colorado Government Revenues.

Source: Colorado Legislative Council Staff, p. 12.

The ratchet-down effect, probably the most glaring unintended consequence of TABOR, permanently reduced Colorado's allowable revenues for future years. This effect was expected to be especially burdensome because as the state experienced population and inflation growth, a growing number of people would need state services at a higher cost. To address this difficulty, Legislative Council suggested a constitutional amendment to the voters to eliminate the ratchet-down effect of TABOR.

At the time, fourteen states used personal income in determining allowable revenue or spending limits. Legislative Council offered, "Should the General Assembly decide that the current TABOR limit factors are not the most appropriate indicators for limiting government revenues, it could consider a constitutional amendment to use the annual percentage change in personal income as the growth limit on state revenue" (Legislative ix).

Continuing to increase General Fund appropriations by six percent consumed an increasing amount of total revenues allowable under TABOR. To address this, Legislative Council suggested that the General Assembly could make the appropriations limit the same as the TABOR limit so that the two limits would move simultaneously.

5.3.2 Fiscal Emergencies

Forty-five states have reserve funds available for use during fiscal emergencies, known as rainy day funds, while Colorado does not. Colorado does have two small reserve funds. The first is required by statute and contains four percent of the state's General Fund appropriations. The second is constitutionally required and contains three percent of total TABOR revenue. Legislative Council provided two specific options should the General Assembly wish to create a rainy day fund. First, the General Assembly could have sought voter approval to change the constitutional reserve into a rainy day fund, and asked voters for permission to retain surplus revenue for such a fund. Use of the fund could have required a supermajority vote, and limits could have been placed on the percentage of the fund to be used at one time. Second, the General Assembly could have sought voter approval to allow savings to be exempt from TABOR spending limits up to some specified amount and to require that the money count under TABOR limits when spent. Colorado is still without a substantial rainy day fund.

5.3.3 Property Taxes

School funding is affected by property taxes and state funds. State funds are used to supplement local funding sources, which is made up mostly of property taxes, and the amount provided under the school finance act. Legislative Council reached three conclusions about Colorado's property tax system. The first conclusion was that constitutional limits held down property taxes in Colorado. Second, the requirement to revalue property every two years created a volatile pattern of growth in taxable property, and property taxes did not generate enough revenues to reach the limits allowed by law. Third, low property taxes burdened the state and forced increase funding in the school finance act over time, which put increasing pressure on the state budget.

Legislative Council offered the General Assembly diverse options for modification of the property tax system to make it more flexible during downturns. First, the General Assembly could have asked voters to allow the legislature to set property taxes for school finance. Second, the General Assembly could have asked voters to restore the floating mill levy for schools within certain limits. Third, the General Assembly could have asked voters to make the constitutional school finance provisions consistent by reducing the Amendment 23 requirement for one additional percentage or by increasing the TABOR limit to allow for the one additional percentage throughout FY 2010-11. Fourth, the General Assembly could have addressed the state's biennial reassessment cycle in the context of TABOR's annual limits by changing the cycle for reassessing property or by modifying the calculations of the limit to account for the two-year's worth of growth in values.

5.3.4 Amendment 23 and State Fiscal Issues

Legislative Council concluded, "Since Amendment 23's passage, the economic downturn has resulted in a number of unanticipated consequences" (Legislative xi). Declining income taxes and revenues affected the General Fund's ability to support the appropriation necessary to develop a substantial base in the State Education Fund, and reduced the cushion available in the State Education Fund to support mandatory funding increases. The result was increased strain on the General Fund as it was used to support

Amendment 23's rigid funding requirements. Legislative Council suggested that the General Assembly could ask voters to increase revenue, either by raising taxes or further reducing taxpayer refunds, or lessening the spending requirements outlined in Amendment 23 (Legislative xii).

5.4 Referendum C

On April 18, 2005 the Colorado General Assembly approved HB 05-1194, more commonly called Referendum C, which was submitted to voters in the election of that the same year. On November 1, 2005, voters consented to a five-year time-out from TABOR when they approved Referendum C. The measure was approved by 52 percent of Colorado voters, while 50.7 percent of voters rejected Referendum D, the parallel measure to Referendum C which would have allowed the state to borrow up to $2.072 billion for transportation projects, K-12 and higher education buildings, and local fire and police pension obligations ("Referendum C").

Referendum C has three major provisions.[11] First, the measure allows the state to disregard the TABOR formula and spend or save all revenues collected from 2006-2010. Allowable uses for retained revenue include K-12 education, higher education, health care, police and firefighter pension plans, and Department of Transportation programs. Second, the measure eliminates the TABOR ratchet effect by using as the base for the TABOR formula in 2011 the fiscal year in which the state had the highest total revenues between 2006 and 2010, and stipulates that in future years the TABOR limit will be based on the prior year's limit instead of actual revenues. When state revenues fell between 2001-02 and 2002-03, the TABOR limit also fell, which ratcheted down

[11] C.R.S. §24-77-103.6.

prospective allowable revenue retention in future years. When revenues began to increase in 2004, the TABOR ratchet had forced future state revenue limits down by over $1 billion annually. Third, the State Controller is required to report on allowable revenue retention spending under Referendum C.

As a result of Referendum C's passage, the six percent appropriations limit will become the effective limit on state government growth. Spending up to the six percent limit will likely continue in order to prevent reductions in General Fund spending for subsequent years. Should income and sales tax revenues grow at a steady rate, General Fund revenues above the allowable six percent limit will be allocated to fund highways and capital construction.

Summary

During the recession, declining revenues, coupled with the TABOR ratchet-down effect, forced disproportionate budget cuts to state departments. First, programs were prioritized. Those programs constitutionally protected or deemed necessary for public safety were made a top priority. Second, budgets for programs ranked lower in priority were wither reduced or terminated. Third, cash funds were transferred to the General Fund in order to maintain state operations. Ultimately, voters approved Referendum C, which provided a solution to the ratchet-down effect and significant revenue declines.

6. The Role of TABOR During the Recession

6.1 TABOR and Public Services During the Recession

TABOR had been popular during the economic expansion of the 1990s. However, sentiments changed when the recession hit in 2001 and critics focused on TABOR's role in "the worst fiscal crisis in decades." The key problem during the recession was declining revenues, which was compounded by the TABOR ratchet-down effect. Although TABOR surpluses had disappeared and tax revenues continued to decline, state officials were required to make TABOR rebates for the prior fiscal year, while also reducing state spending levels. TABOR proved to be a fiscal accelerator rather than a fiscal stabilizer, exacerbating the state's financial difficulties (Hill et al.). Nobody thought this mattered when the constitutional amendment [TABOR] was enacted in 1992 because it seems natural for revenues to grow from one year to the next (Snell 24).

As revenues declined, Amendment 23 simultaneously required increases in state appropriations for K-12 education. Although proponents of Amendment 23 had anticipated the requirement for increased funding being financed by TABOR surpluses, there were no surpluses (Snell 24). And there was no escape clause either. According to statute, Amendment 23's provisions must be met, but TABOR prevented raising taxes or lifting Amendment 23's requirements even temporarily without voter approval.

In short, TABOR and Amendment 23 served opposing sides of a fiscal vise that squeezed the state budget during the recession and impeded necessary adjustments for recessionary cycles. During the 2003-2004 legislative session, alleviating accumulated pressure from the fiscal vise squeezing the state budget was the most urgent issue lawmakers' faced (James and Wallis 16). Ultimately, other areas of the budget were cut in order to fund mandatory increases in K-12 education. Such cuts were concentrated in a few state programs, primarily higher education and social welfare programs (Poulson, "Colorado's" 17).

According to the National Conference of State Legislatures, the TABOR amendment itself is only one strand of a tangle of Colorado constitutional and statutory provisions that have generated a constitutional dilemma. Limits on revenue and spending and constitutional requirements for spending growth have created a structural deficit. TABOR, however, is the most important strand of the tangle (Snell 24). This position is aligned with much of the literature on Colorado's TELs and the recession.

Poulson notes, it is impossible to simultaneously achieve the desired ends of each of the fiscal provisions of the Colorado Constitution; some provisions require a ratcheting down of government revenue and spending, while others require a ratcheting up of spending. To satisfy each of these provisions would require deficit spending during recessions, which is exactly when there is a revenue shortfall. And, in the long run, the provisions build a structural deficit into the budget. Constitutional provisions that require a balanced budget prohibit both outcomes (Poulson, "Colorado's" 20).

The authors of TABOR wanted to limit the growth of government in Colorado. In 1991, Colorado's state and local taxes as a percentage of income ranked 25th according to The Tax Foundation. In the decade following TABOR's passage, Colorado fell on the list to 47th. TABOR has reduced, not merely maintained, the growth of Colorado's government relative to the economy ("Flaws" 5). In 2003, Colorado's Fiscal Policy Institute asserted, "TABOR functions to limit government growth when robust revenues would normally enable it to catch up with a backlog of needs, and it ratchets down the base when revenues fall below an artificial and inappropriate formula. In a modern society, this trend is unsustainable since state government is increasingly holding up an ever-growing part of the social and economic safety net in America ("Flaws" 5).

While proponents of TABOR assert that it has functioned to reduce the size of government in Colorado, opponents question the impact TABOR has had on the state's public services, especially during the recession. Overall, opponents contend that TABOR adversely affected some of the state's public services by magnifying the effects of the recession on the Colorado budget and forcing over $1 billion in cuts (e.g., Bradley and Lyons). Significant cuts were made in the following areas:

- Non-emergency Medicaid Transportation (cut by nearly 2/3), which left many Medicaid participants without transportation to and from medical care sites;
- Medicaid services to legal immigrants, including pre-natal care;
- Affordable housing loans and grants;
- Low-income preschool slots were cut in half;
- Aid to the Needy Disabled; and
- Mental health services ("TABOR had" 3).

Cuts to the six largest state departments were smaller relative to the cuts made for other departments. Some of the departments experienced significant General Fund reductions, ranging from 20 percent up to 85 percent. Between 2001 and 2003, total funding for seven departments grew faster than population and inflation, while all other departments experienced cutbacks on a real, per capita basis ("State Budget" 9). Some of the departments that lost General Funds were able to maintain services by switching to alternative funding sources, such as federal funding or cash funds. Departments unable to take such a course of action were forced to reduce service levels. Figure seven indicates how total state funds were appropriated to each department between FY 2000-01 and FY 2004-05.

Department	**% Change from FY 00-01 – FY 04-05**	**% of Total Funding to Department**
State	94.8	0.2
Education	34.3	24.8
Local Affairs	32.3	1.3
Public Safety	32.2	1.6
Health Care Policy	31.3	21.8
Personnel & Administration	19.6	1.3
Corrections	15.5	4.0
Judicial	12.3	2.1
Natural Resources	10.4	1.3
Military/Veterans Affairs	10.2	0.9
Public Health & Environment	9.4	3.8
Revenue	9.2	0.3
Law	8.8	12.0
Higher Education	8.6	1.0
Regulatory Agencies	5.3	0.5
Agriculture	-.08	0.2
Treasury	-2.8	1.9
Governor	-4.0	0.3
Legislature	-4.2	0.2
Human Services	-6.6	12.0
Transportation	-34.1	6.6

Figure 7: Departmental Appropriation Breakdown of All Funds (General, Cash Funds, Cash Funds Exempt, and Federal Funds) Between FY 2000-01 and FY 2004-05.

Source: Colorado Fiscal Policy Institute, "State Budget Cuts, 2001-05," November 2004, p. 5.

The six largest departments are, in order: Education; Health Care Policy and Financing; Higher Education; Corrections; Human Services; and Judicial. These departments are caseload driven, and General Fund appropriations to them are based largely on their budgetary needs in meeting caseload demand. Economic conditions, demographic factors, and constitutional, statutory, and federal requirements drive caseloads. The Colorado Constitution mandates the provision of the public school system for all residents between ages 6 and 21. Statutory criminal sentencing laws and parole requirements influence prison caseloads. Numerous programs within the six major departments involve matching federal funds, and the receipt of federal funds typically entails a host of stipulations concerning the populations to be served.

Economic conditions and population growth are also considerable caseload drivers. Economic upswings are typically correlated with increased state revenues, population growth, and inflation, and these factors both increase costs to departments and expand caseloads. During economic upswings, caseload growth is typically greater for the Dept. of Education, Dept. of Health Care Policy and Financing, Dept. of Human Services, Dept. of Corrections, and the Judicial Department. A robust economy attracts people to the state, which increase K-12 enrollment and weigh on the Dept. of Education. Costs of medical services and supplies already persistently exceed the inflationary rate and continue to rise during economic upswings, which, in turn, increase costs overall to the Departments of Health Care Policy and Financing and Human Services. Population growth during periods of economic prosperity is associated with increased case filings, which burden both the Dept. of Corrections and the Judicial Dept.

Economic downturns are typically correlated with decreased state revenues, population decline, and inflation, and caseload growth typically expands as people are adversely impacted by the characteristics of a slowing economy. More specifically, during such periods, caseload growth is typically greater for the Departments of Higher Education, Health Care Policy and Financing, and Corrections and Judicial: more people enroll in higher education when job availability decreases, which increases costs for the Dept. of Higher Education; more people become indigent during downturns, which drives Medicaid caseloads for the Dept. of Health Care Policy and Financing; and increased crime levels during downturns drives caseloads for the Departments of Corrections and Judicial.

The assessment of TABOR, Amendment 23, the Gallagher Amendment, and other Fiscal Issues prepared by Colorado Legislative Council outlines a number of ways in which TABOR influenced funding for departments during the recession. First, regarding Gallagher and TABOR, the report indicates that the combination of the Gallagher amendment and TABOR effectively placed the burden of increased funding for K-12 education on the state. TABOR precludes raising the mill levy without voter approval, and the slow growth in property tax revenue made supplemental state funds compulsory. TABOR limited allowable tax revenue quantities school districts could receive, which further shifted the funding burden to the state. The heightened funding burden for K-12 education reduced funding available overall for the departments (Legislative 10 of Appendix B).

Second, the report considers caseload growth for departments and the role of TABOR. For example, caseloads and probationers significantly drive Judicial Department expenditures. Should growth in caseloads and probationers exceed population growth (assuming inflation affects the department and the state the same), department expenditures may be greater than the TABOR limit, which pressures the

General Assembly because the TABOR limit imposes a ceiling on revenues overall (Legislative 44 of Appendix B). Similarly, the number of prisoners and the costs of imprisonment determine expenditures for the Dept. of Corrections. If prison population growth exceeds the state's general population growth, department expenditures may be greater than the TABOR limit, which puts pressure on other areas of the budget and other departments reliant on General Funds. This was the scenario during the recession. Funding for the Dept. of Corrections did increase considerably during the recession and resulted in funding decreases in other areas of the budget. In every fiscal year since FY 1989-90, growth in the Colorado prison population has been greater than that of the general population.

6.2 The Case of State Mental Health Services During the Recession

The Colorado Department of Human Services (DHS) is responsible for the provision of non-medical public assistance and welfare services. DHS programs include: cash and food assistance, child support enforcement, child welfare, rehabilitation services, veterans services, alcohol and drug treatment, services for the aging, care for the mentally ill, developmentally, disabled, and juvenile offenders. Colorado's Mental Health system, which is administered by the Division of Mental Health, a division within the Colorado Department of Health and Human Services Office of Behavioral Health, provides essential services to some of the state's most vulnerable citizens. Mental health patients rely on treatments, which are often crucial in order to prevent the infliction of harm to patients themselves or to others.

In order to provide the bulk of its services, the division contracts with mental health centers throughout the state. The most serious cases are serviced at two Colorado

Mental Health Institutes located in Pueblo and Fort Logan. There are 17 community mental health centers and six specialty mental health clinics with which the DHS contracts. Funding for the community mental health program is made up of state funds matched by Federal Medicaid funds at a rate of about 50 percent. Between FY 1990-91 and FY 1996-97, General Fund appropriations to the community mental health system increased at an average annual rate of 5.6 percent, from $31.9 million to $46.7 million. Funding increased significantly in FY 1998-99 with implementation of the Medicaid Mental Health Capitation program. While General Fund allocation to the department increased for the following five years at a rate of 3.3 percent, it decreased due to the revenue shortfall.

The Medicaid Mental Health Capitation program is a managed mental health care system that is funded mainly by Medicaid. The program covers eight regions within Colorado, and the management of the program is carried out by individual organizations in each region, known as Mental Health Assessment Services Agencies (MHASA). The state pays each MHASA a monthly flat fee per Medicaid patient enrolled, and most Medicaid patients in Colorado are enrolled in the program. Program funding is largely determined by Medicaid eligibility, which increased 9.5 percent between FY 1998-90 and FY 2003-04 (Legislative 36 of Appendix B).

Mental health institutes are charged with providing care to patients who have very serious mental illnesses. Institutes received annual General Fund appropriation increases at a rate of 1.4 percent (from $52.3 million to $62.5 million) between FY 1990-91 and FY 2003-04, while Medicaid funding decreased from $13.3 million to $3.3 million during the same period (Legislative 36 of Appendix B).

Colorado's broader mental health system suffered funding cuts during the recession, which led to treatment reductions. In a February 2005 report entitled, "An Analysis of Recent Trends in Colorado's Mental Health System," the Division of Mental Health acknowledges that the recession forced departmental budget cuts, outlines how the budget cuts were made, and presents the following key findings:

- The number of Medicaid eligible persons receiving services declined;
- 16,378 fewer persons were reported served from FY 2001 to FY 2004. Although 11,195 fewer non-Medicaid persons were served, there were also 5,183 fewer Medicaid individuals reported served in spite of increases in Medicaid eligibility over that period;
- The public mental health system no longer reported serving an equal number of non-Medicaid persons. 10,461 fewer non-Medicaid than Medicaid persons were reported served in FY 2004, which is a reversal of FY 2001 when 878 more non-Medicaid persons were reported served;
- Non-Medicaid federal and State General Funds shrank as a percentage of total, reported revenue from 19.1 in FY 2002 to 16.8 in FY 2004; and
- The average funding per Medicaid eligible declined 24.7 percent from FY 2002 to FY 2004;
- The level of severity of those reported served increased from FY 2001 to FY 2004. Cases of children and adolescents with serious emotional disturbances increased from 64.76 percent in FY 2001 to 74.20 percent in FY 2004. At the same time, the percentage of adults with serious and persistent mental illnesses increased 6.68 percent; and

- Two-thirds of all units of service reported were delivered to Medicaid persons in FY 2004. In FY 2001, 48 percent of all units of services reported were delivered to Medicaid persons (2-3).

In outlining how the budget cuts were made, the February 2005 report (2-19) indicates that between FY 2002 and FY 2003, the total quantity of General Fund dollars apportioned for the provision of services to adults and children with serious mental illnesses was reduced from $18,777,197 to $15,671,434, a decrease of 16.54 percent. Between FY 2003 and FY 2004, General Funds were reduced by $1,601,635, a decrease of 10.22 percent. In sum, between FY 2002 and FY 2004, total General Funds were decreased by $4,707,398, which represents a total decrease of 25.06 percent. During this period, the number of long-term care beds in the state's two mental health institutes was also reduced. The Fort Logan Mental Health Institute reduced residential unit beds by 16 beds, adult unit beds by 27, and eliminated an after-care treatment program. Pueblo Mental Health reduced adolescent unit beds by eight and adult unit beds by 27.

Between FY 2002 and FY 2004, the total quantity of General Fund dollars apportioned to the Medicaid Mental Health Capitation program were also reduced, even though the number of caseloads increased during this period. In FY 2002, the program received $184,906,860 in General Fund dollars. In FY 2003, General Fund dollars appropriated for the program decreased to $144,704,276. In FY 2004, General Fund dollars did increase, but only by 1.72 percent. Between 2002 and 2004, the total number of eligibles (caseloads) grew by 30.58 percent, while funding per eligible decreased by 24.73 percent during this period ("An Analysis" 3-4).

Between 2001 and 2004, General Funds were reduced by over 10 percent for alcohol and drug abuse programs, which relates to mental illness since mental illness and substance abuse are correlated. Some mental health and drug abuse programs were eliminated altogether including the:

- Early Intervention Program;
- Mental Health Treatment Program for Detained Youth;
- Early Childhood Mental Health Program; and
- Community Mental Health Programs for uninsured, non-Medicaid clients ("TABOR Issue").

During the same period, funding for mental health services in all state detention facilities was eliminated, which included funding for a secure juvenile. The Bell Policy center reported that, "At a time when state budget cuts have eliminated many treatment programs for juvenile delinquents, the Colorado Division of Youth Corrections recently reported that 24 percent of all juveniles in the justice system have been diagnosed with a serious mental illness facility" ("TABOR Issue").

According to David Iverson, M.D., former Chair of Governor Owens' Advisory Board for Mental Health and the Law, described the effects of TABOR on the public mental health system, "The TABOR ratchet effect has squeezed a mental health system that was already struggling to the point where it is no system at all. The problems outlined are the result of a sick system that without any doubt has been significantly eroded by the effects of TABOR and the budget crisis. The social safety net and the social contract are in tatters" (191).

6.3 The Case of Higher Education During the Recession

The Department of Higher Education also faced serious budget complications during the recession. Higher education funding was reduced by 22 percent between 2002 and 2005, while tuition increased 30 percent during the same years. A former President of the University of Colorado noted in 2004, "Public higher education is at a critical juncture. A combination of recent budget cuts and increasing costs has put all of our budgets in serious jeopardy…there is a very real threat that Colorado will not be able to provide any public funding for higher education by the end of this decade" (Hoffmann). According to a *Rocky Mountain News* article, in 2008, state appropriations for some colleges – including the University of Colorado, Colorado State University, and the University of Northern Colorado – are still below pre-recession levels because the six percent limit prevented legislators from ramping up spending when the recession ended" (Morson A1).

The Dept. of Higher Education provides educational opportunities for Colorado residents through a system of 26 state campuses, two district junior colleges, and four vocational schools. While traditionally funding for the department has been primarily from General Funds and tuition payments, in FY 2002-03 cash funds and increased tuition rates served as primary revenue sources. Enrollment growth, inflation, performance measures, and tuition are the main factors that drive higher education expenditures. Even low levels of student enrollment increases can drive great need for General Funds, and, like many other departments, higher education needs base funding increases each year just to keep pace with rising costs.

During the recession, areas of the budget that lacked constitutionally mandated funding increases, areas that were not matched with federal funds, such as Medicaid, and areas that were not driven by statutes that mandate funding, such as criminal codes that mandate incarceration, were especially vulnerable to budget cuts. Higher education is a prime example of this since it did not match these criteria. Further, higher education sustained a disproportionately larger General Fund reduction because it is generally considered a balancing mechanism of the budget, and it is perceived that higher education has the ability to generate new revenue through tuition increases ("Supporting" 3). Between FY 2002-03 and FY 2005-06, Colorado policymakers cut General Fund appropriations for higher education by $177.4 million ("Update"). Figure eight indicates the share of the General Fund received by the Dept. of Higher Education between 1990 and 2004.

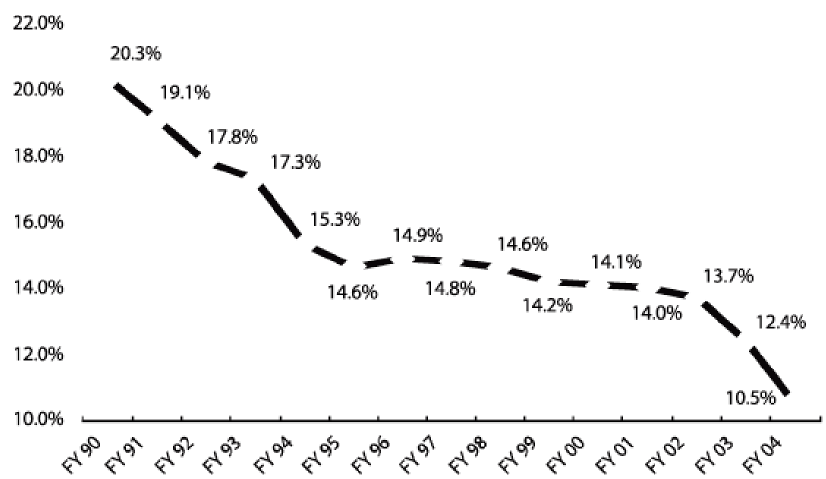

Figure 8: Change in the Share of General Fund Revenues Allocated to the Department of Higher Education.

Source: Colorado State University, "Supporting Excellence: The Funding Challenge for Colorado Higher Education," February 2004, p. 3.

While General Fund appropriations for higher education decreased, tuition rates increased. However, tuition increases did not provide enough revenue to offset the decline in General Funds. Figure eight outlines the state funding changes for higher education during the recession. The Bell Policy Center explains:

- Between 2001 and 2004, state funds for higher education declined 32 percent;

- In FY 2003-04, state fund appropriations for higher education reached their lowest level in over 20 years;
- In 2004, Colorado ranked 45th nationally in providing an opportunity for low-income students to attend college and 47th in postsecondary enrollment rates for minority young adults (age 18-24);
- In 2004, the Colorado Commission on Higher Education estimated that the state need-based financial aid programs covered less than 7 percent of student demonstrated financial need; and,
- In 2004, Colorado ranked 48th nationally for state funds for higher education per $1,000 of personal income ("Colorado TABOR").

Year	State Funds for Public Colleges	% Change from Prior Year	Funding per Colorado Student
2000-01	$613 million	3.5	$5,228
2001-02	$618 million	0.8	$5,062
2002-03	$566 million	-8.4	$4,330
2003-04	$496 million	-12.4	$3,632
2004-05	$491 million	-1.0	$3,545
2005-06	$534 million	8.0	$3,918
2006-07	$579 million	8.4	$4,337
2007-08	$628 million	8.4	$4,640
2008-09	$680 million	8.3	n/a

Figure 9: Public Higher Education Funding Changes between FY 2000-01 and FY 2008-09

Source: "Colorado Colleges in a Hole," *Rocky Mountain News*, April 28, 2008

Historically, Colorado funding for higher education has not traditionally ranked highly relative to other states. In 2002, cuts to higher education were $52 million, and cuts persisted until 2005. Cuts to higher education were significant for two main reasons.

First, funding increases are not mandated constitutionally or statutorily. When revenues declined, higher education funding cuts were used offset funding increases elsewhere in the budget. Second, TABOR and Colorado's other limitations restricted revenue retention and governed spending decisions.

While Referendum C helped the Department of Higher Education to overcome some of the financial setbacks it has incurred, additional resources are still needed.

According to a Colorado State University report prepared in 2004 on higher education funding:

> The decline in state support for Colorado colleges and universities is exacerbated by constitutional limitations, including TABOR. Although perhaps unintended, tuition revenue, paid by students and parents to support a college education, is considered TABOR revenue, and it is therefore subject to the same restrictions as revenue derived from taxes…we must support innovative and creative programs that allow funding to follow students. But such programs are not sustainable within the current constitutional limits placed on our state by the TABOR Amendment and other measures, since there will be no significant state General Fund left to invest in any form of public higher education ("Supporting").

Summary

Although, voters approved TABOR as a measure to limit the growth of government, it has had unintended consequences that posed great difficulties during the recession. First, the TABOR ratchet effect limited state revenues drastically and unexpectedly. Second, TABOR interacted with the state's other limitations in such a way that reduced options available to legislators in dealing with the recession. Voter approval was required to lift any of the state's limits, and while TABOR mandated taxpayer refunds, Amendment 23 mandated increased K-12 education spending.

General Fund revenues declined substantially during the recession, which forced budget cuts in order to maintain core state operations. The budgets of fifteen state departments were reduced between FY 2000-01 and FY 2004-05. Notably, budget cuts to the departments of Human Services and Higher Education were considerable. Cuts to the state's mental health system forced service reductions, and cuts to the higher education system forced tuition increases.

7. Conclusion

Prior to the economic downturn, TEL proponents in other states held up Colorado as a model for the benefits of TEL enactment. However, during the recession this changed and Colorado instead became a model for the potential complications these measures can pose for state governments.

Colorado's TABOR Amendment was promoted as a simple way to restrain government growth, which appealed to Colorado's tradition of anti-tax, anti-government sentiments. Although Colorado's TABOR law has functioned to reduce the size of government since it passed with a majority of votes, it had significant unintended consequences that became widely apparent when it compelled a budget squeeze that heavily impacted areas of the budget for which funding was not constitutionally or statutorily mandated. Between 2001 and 2005, TABOR limited the options available to officials responding to the fiscal crisis, conflicted with the state's other limitations, particularly Amendment 23, forced reductions in state services, and forced tuition increases. The passage of Referendum C suggests a mismatch between voter preferences and TABOR's unintended consequences. Further, ambiguities in how TABOR refunds are to be made have allowed legislators to allocate surplus revenues in such a way as to benefit special interests which also constitutes an unintended consequence of the TABOR law.

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