

*Financing Colorado's Future –
An Analysis of the Fiscal
Sustainability of State
Government*

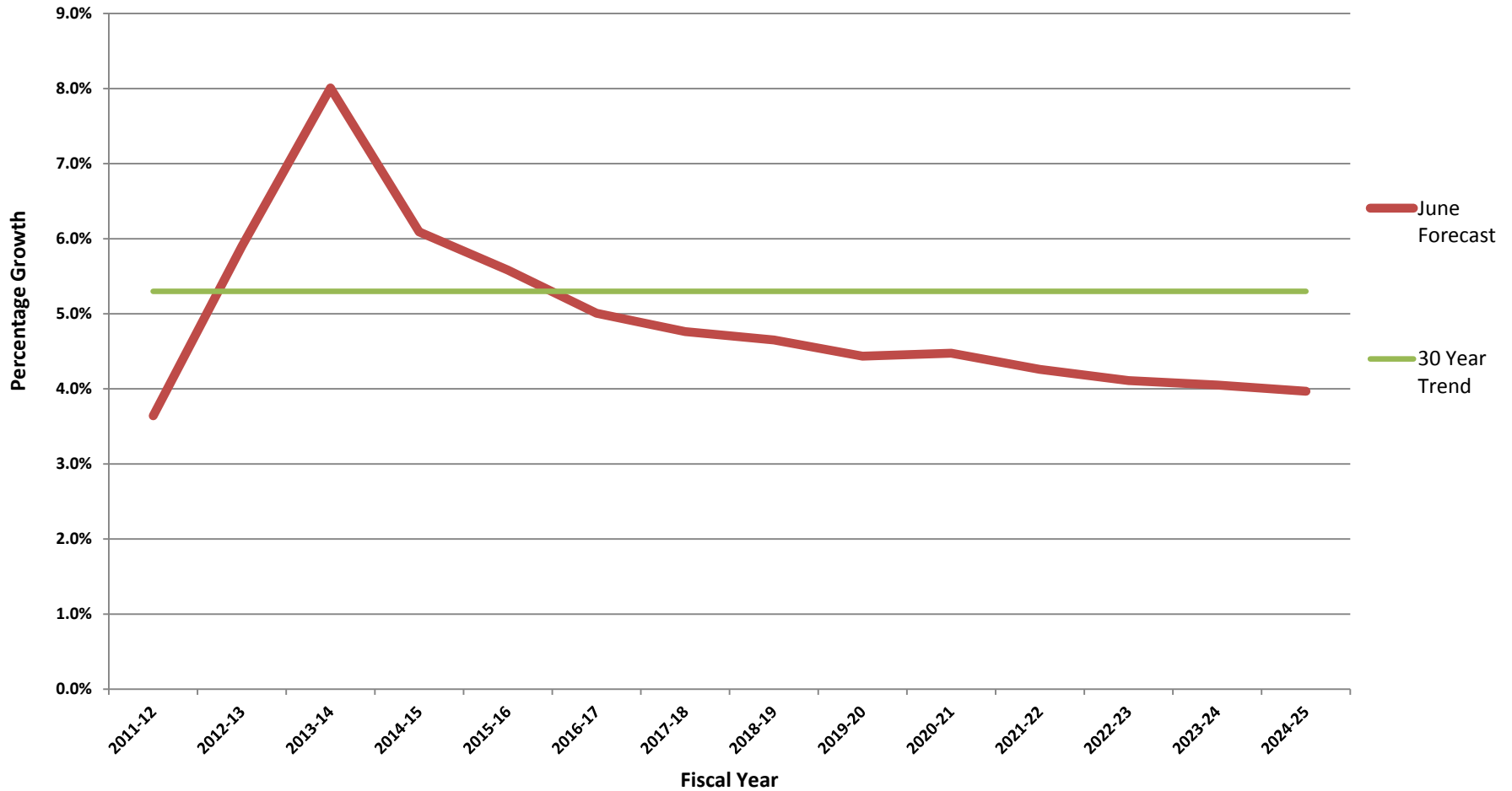


When did the Great Recession Become the Least Interesting Problem Facing Colorado?

Employment Recovery

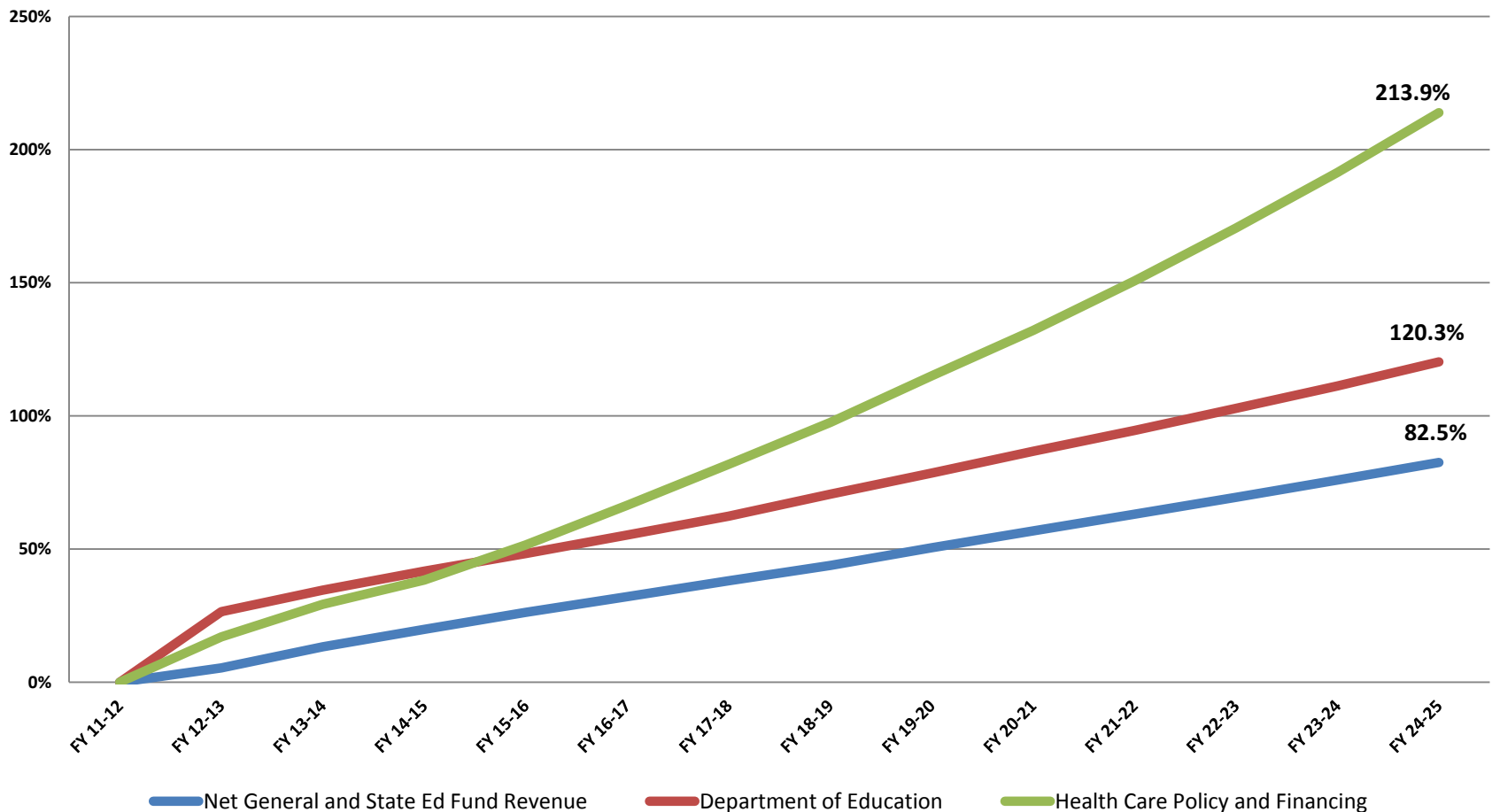


Recovery Will Bring Revenue Growth



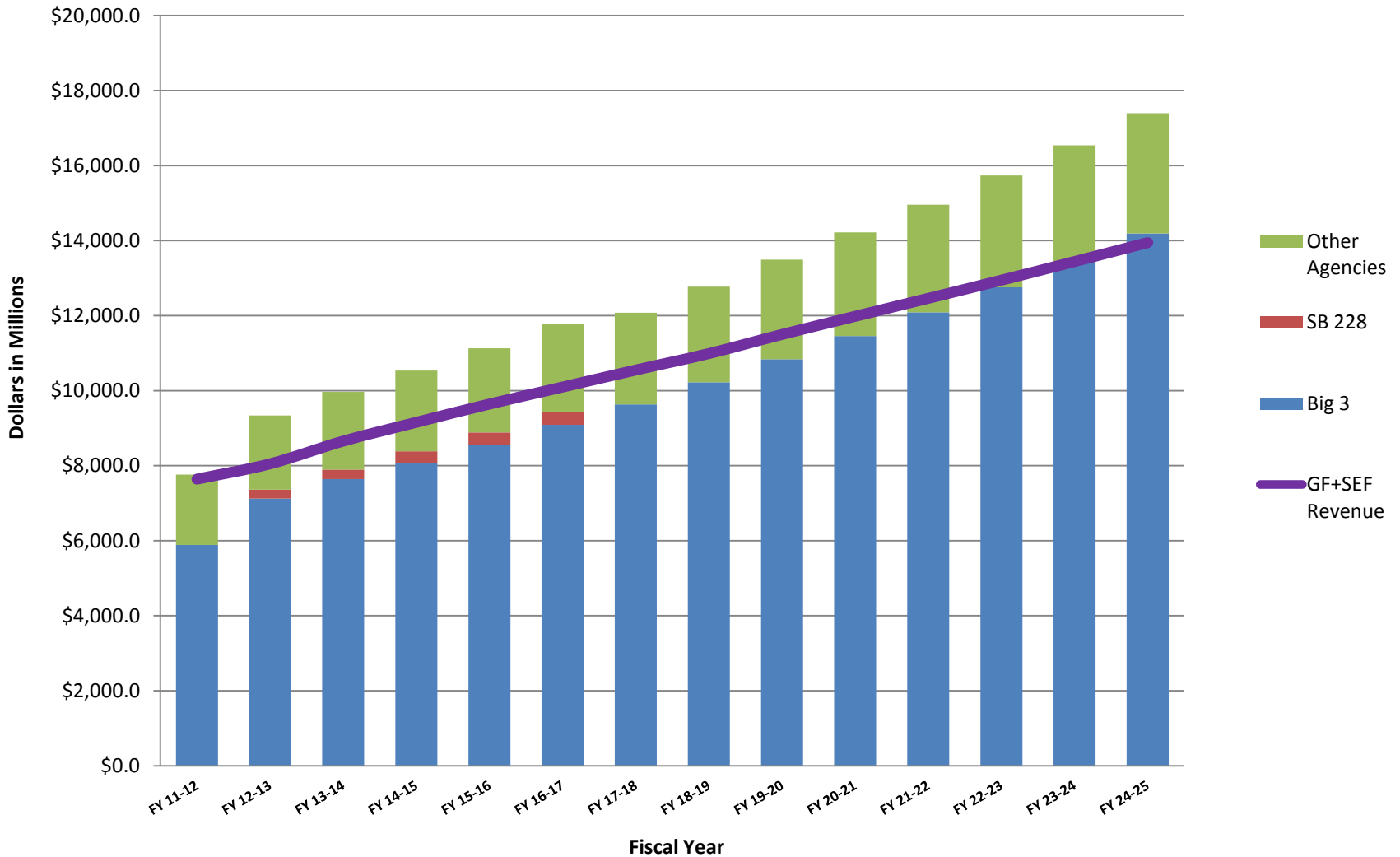
But Colorado's Structural Budget Problems Will Worsen

Cumulative Growth Rates From FY 11-12 through FY 24-25 for General and State Education Fund Revenues and Departments of Education and Health Care Policy and Financing



Due to Medicaid and K-12 Education Forecasts, the Budget Picture Worsens

Comparison of General and State Education Fund Revenue with Expenditures
FY 11-12 through FY 2024-25

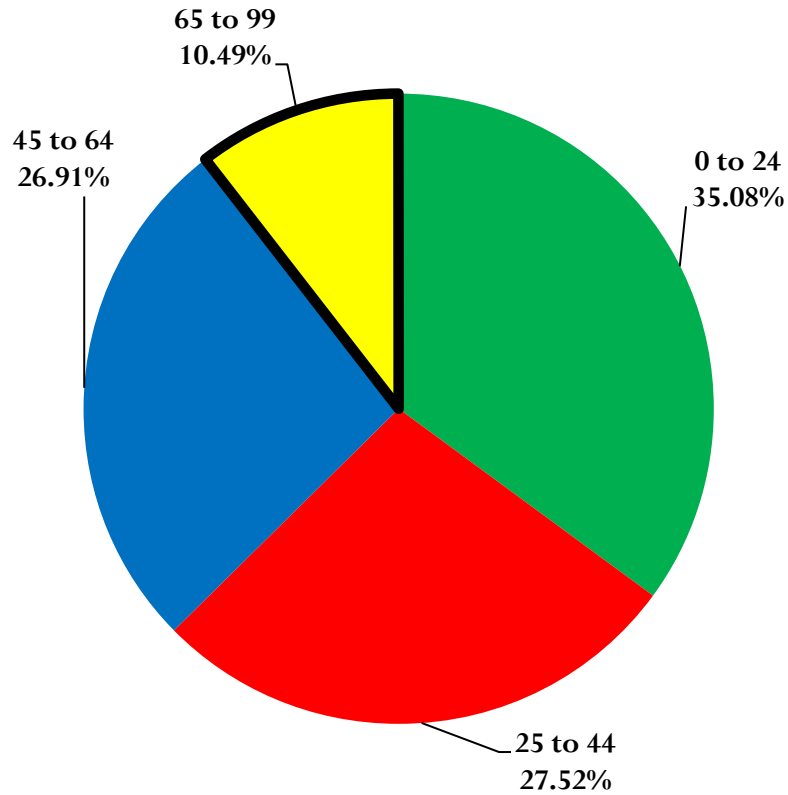


Diagnosis: What is Happening?

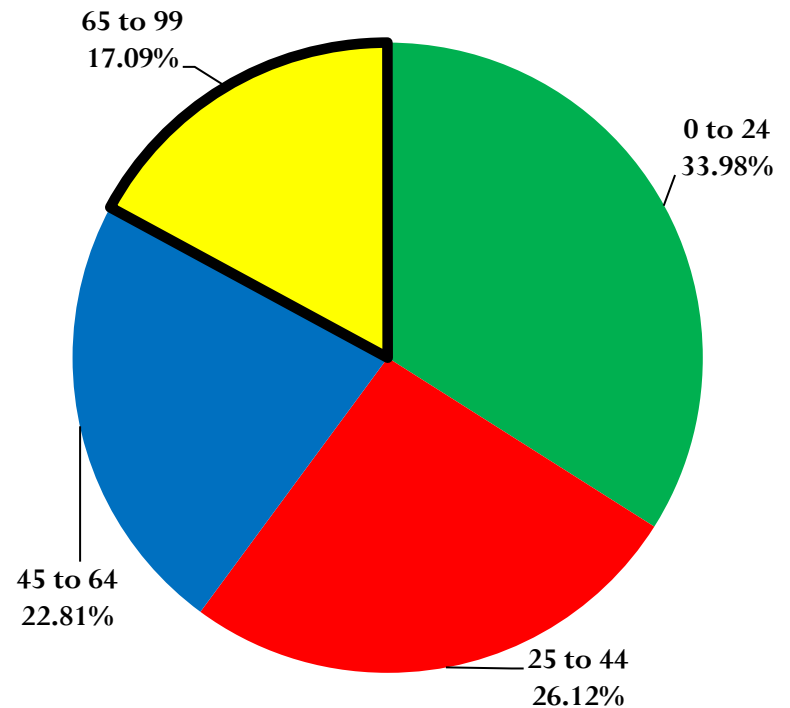
- Structural and demographic changes will affect revenue
- Medicaid growing at 1.7 times revenue
 - Age Demographics
 - Medical Inflation
- System being used to pay for is K-12 failing the state
 - Leakage in local property tax

Colorado is Aging

2010

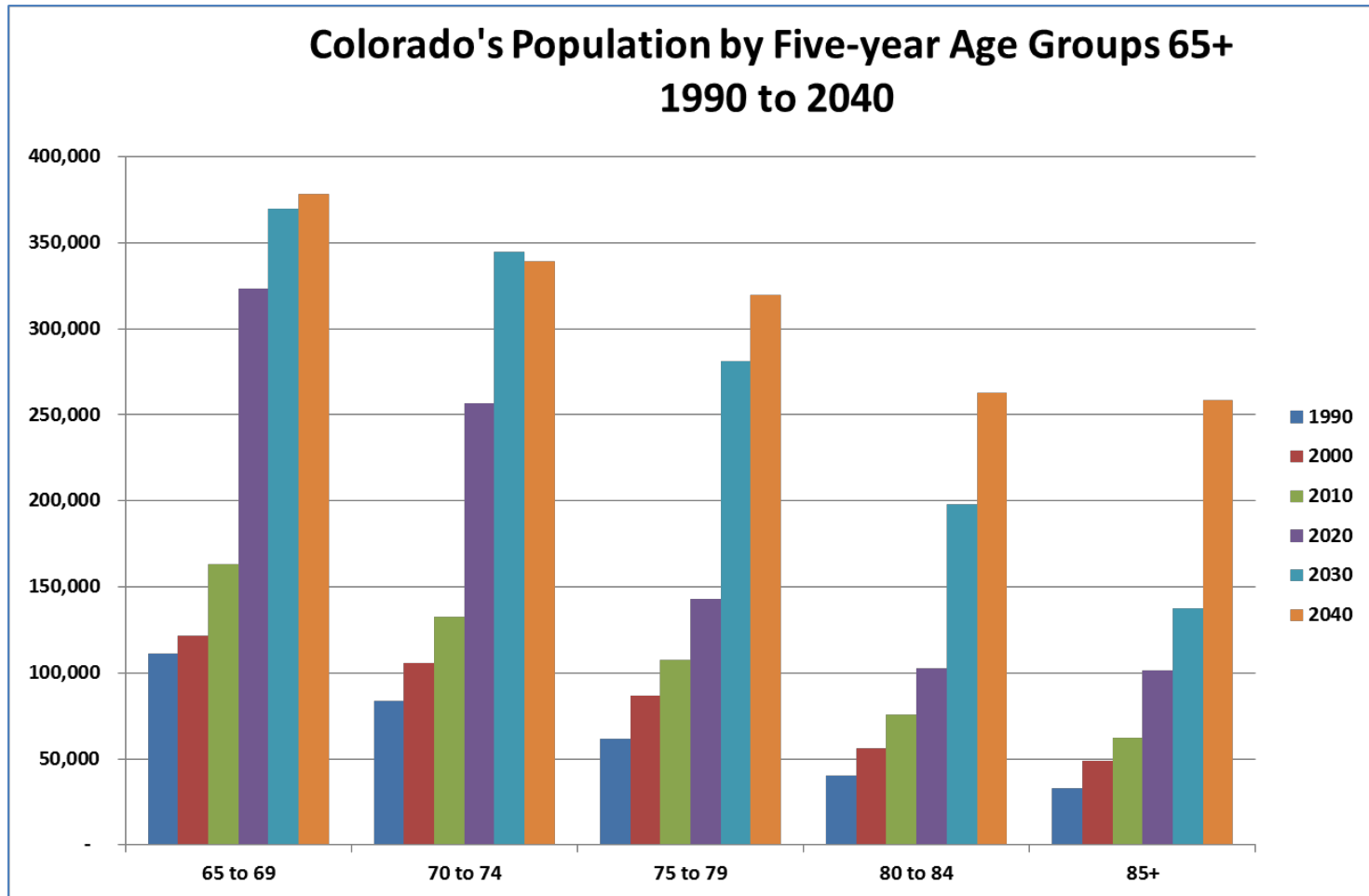


2025



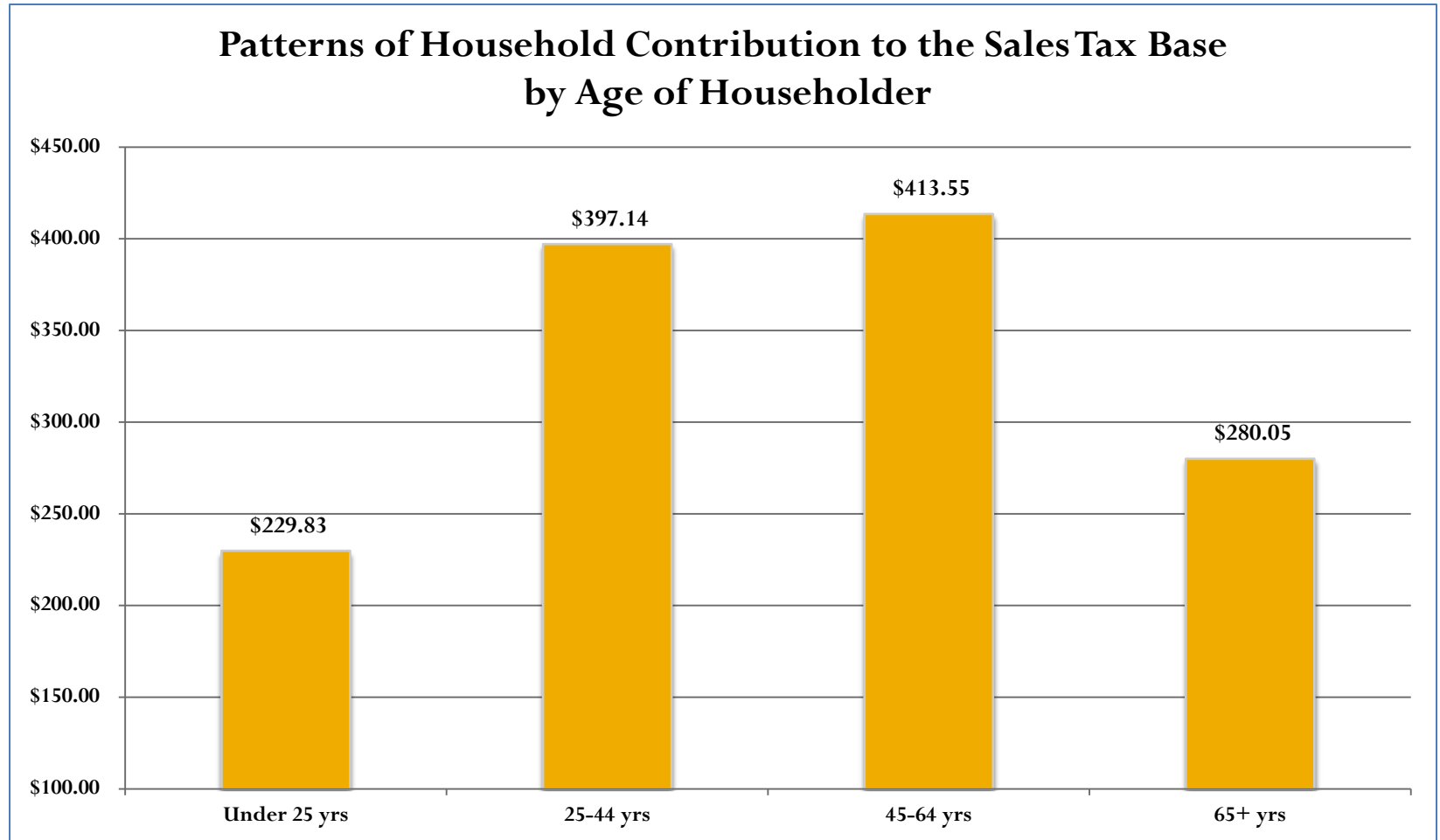
Source: Colorado Demographer's Office

Colorado is About to Become an Older State



Source: Colorado Demographer's Office

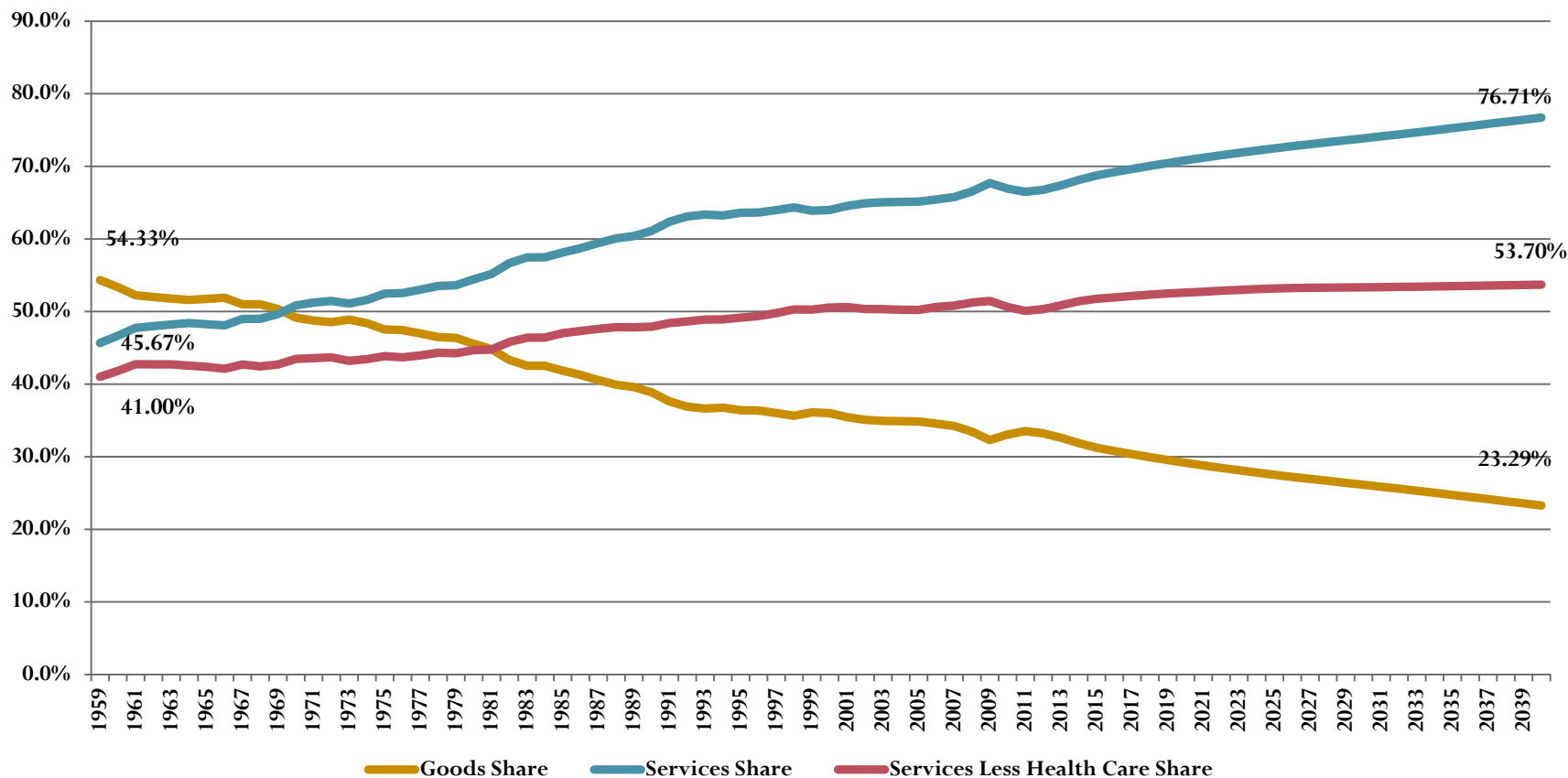
Aging Affects Revenue



Source: Consumer Expenditure Survey, BLS

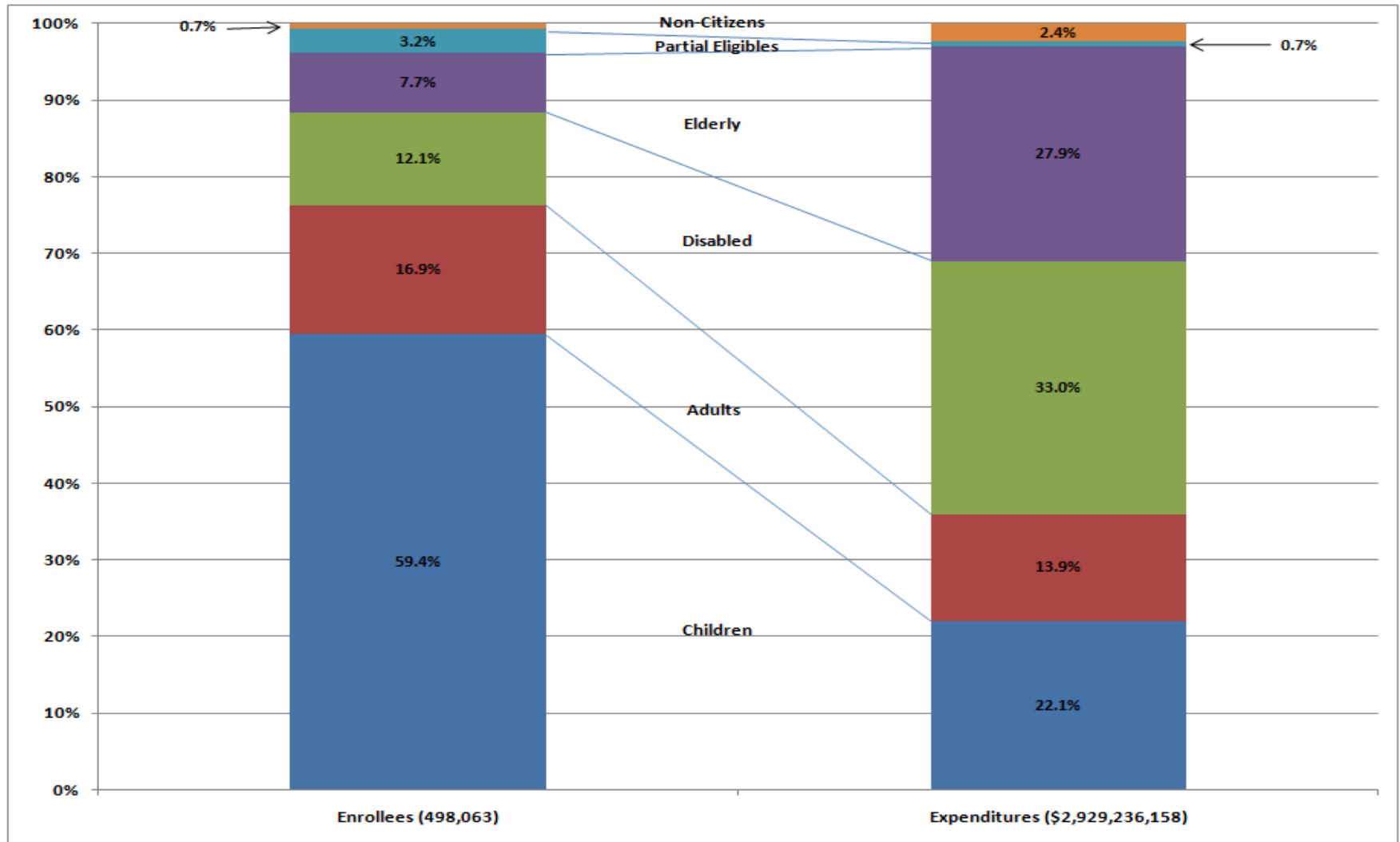
The Economy is Changing

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



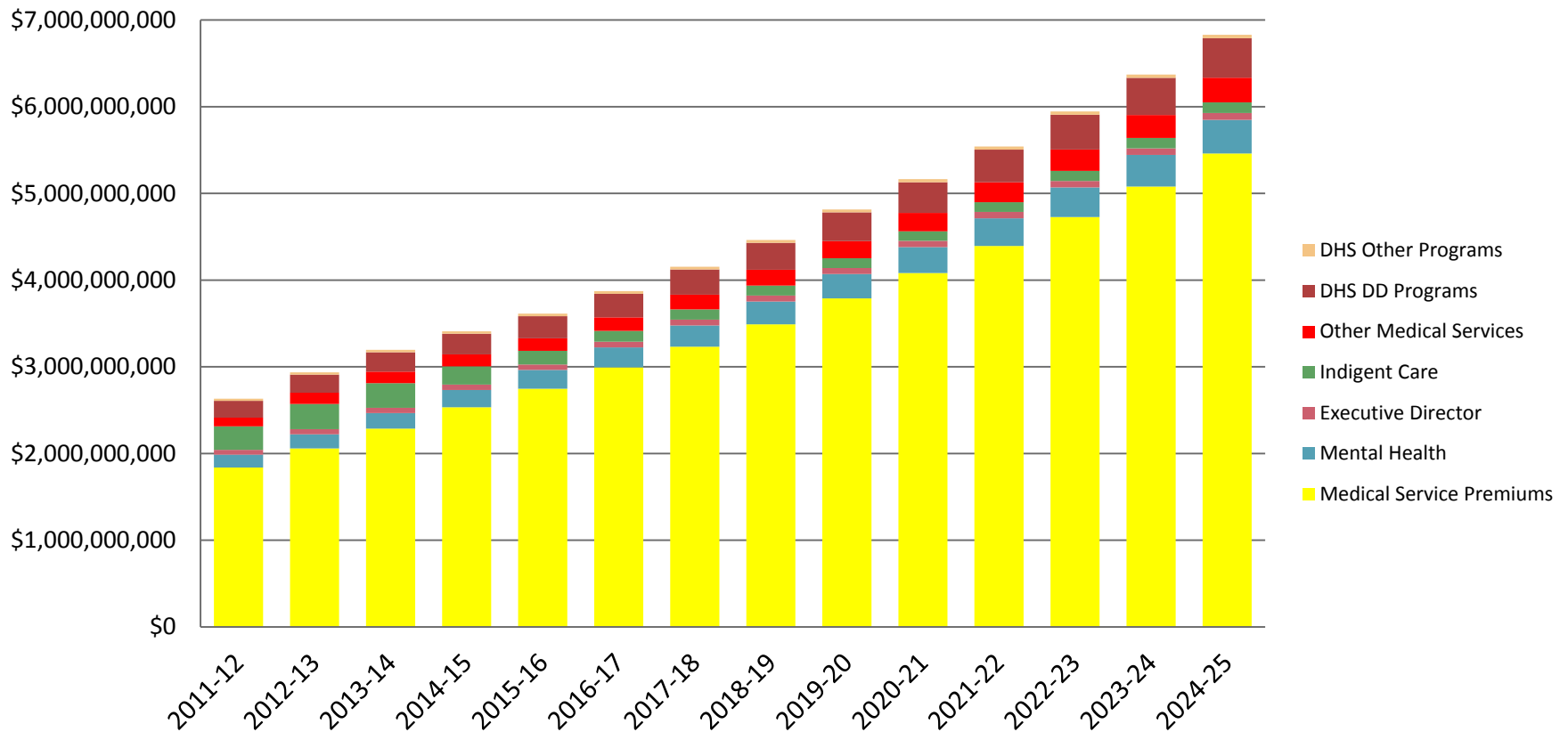
Source: Moody's Economy.com

Aged Care Represents Disproportionate Share of Medicaid Cost (FY 10 Data)

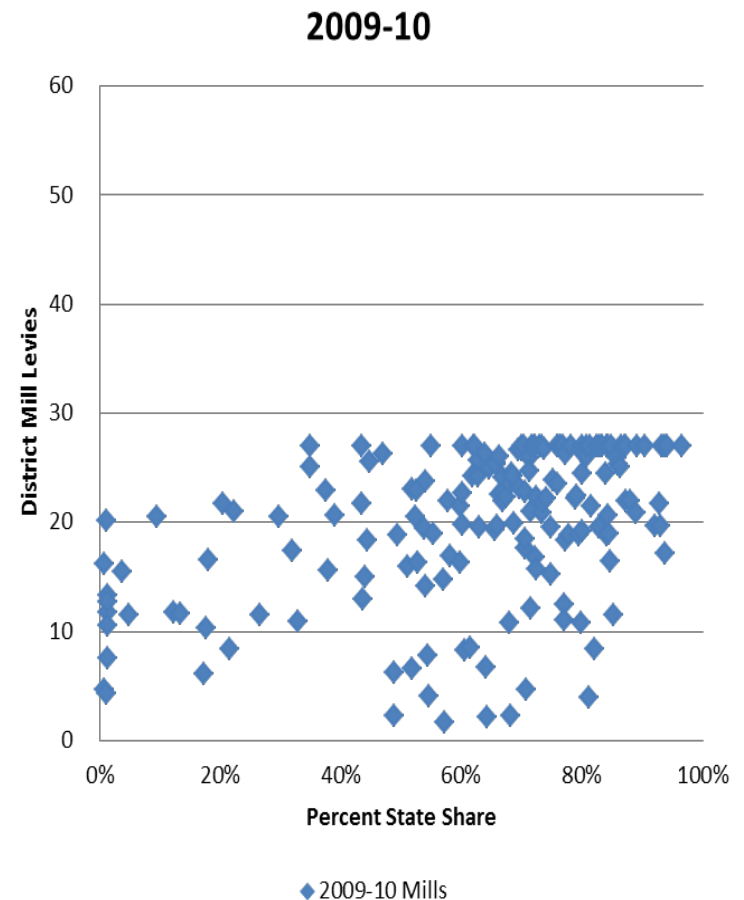
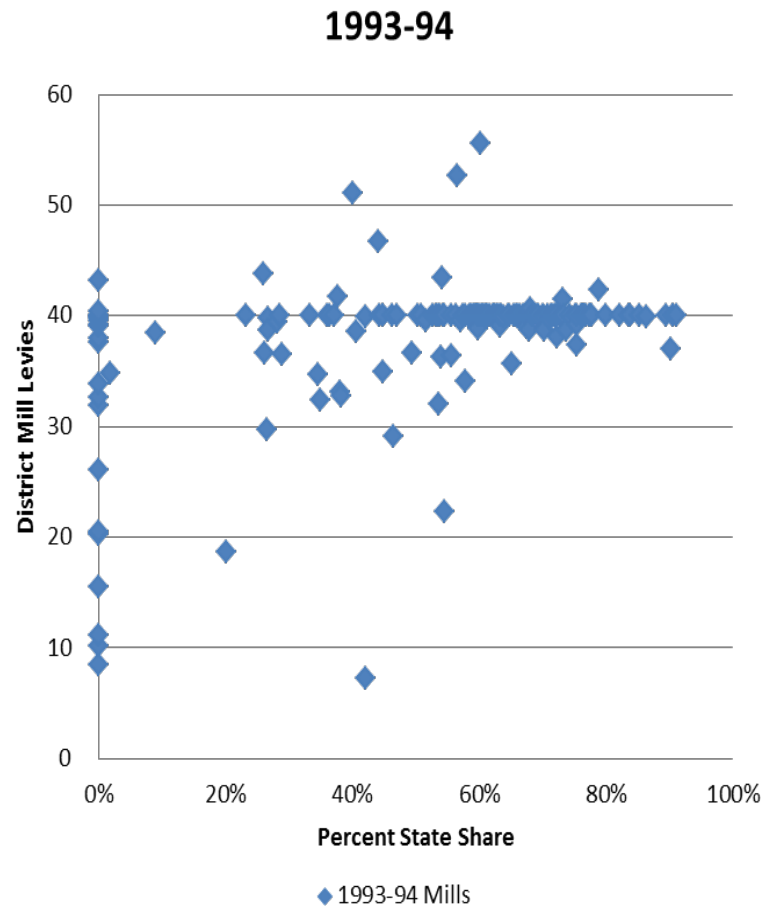


And Aged Care will Drive Medicaid Costs

**State HCPF Expenditures by Division
FY 2011-12 to FY 2024-25**

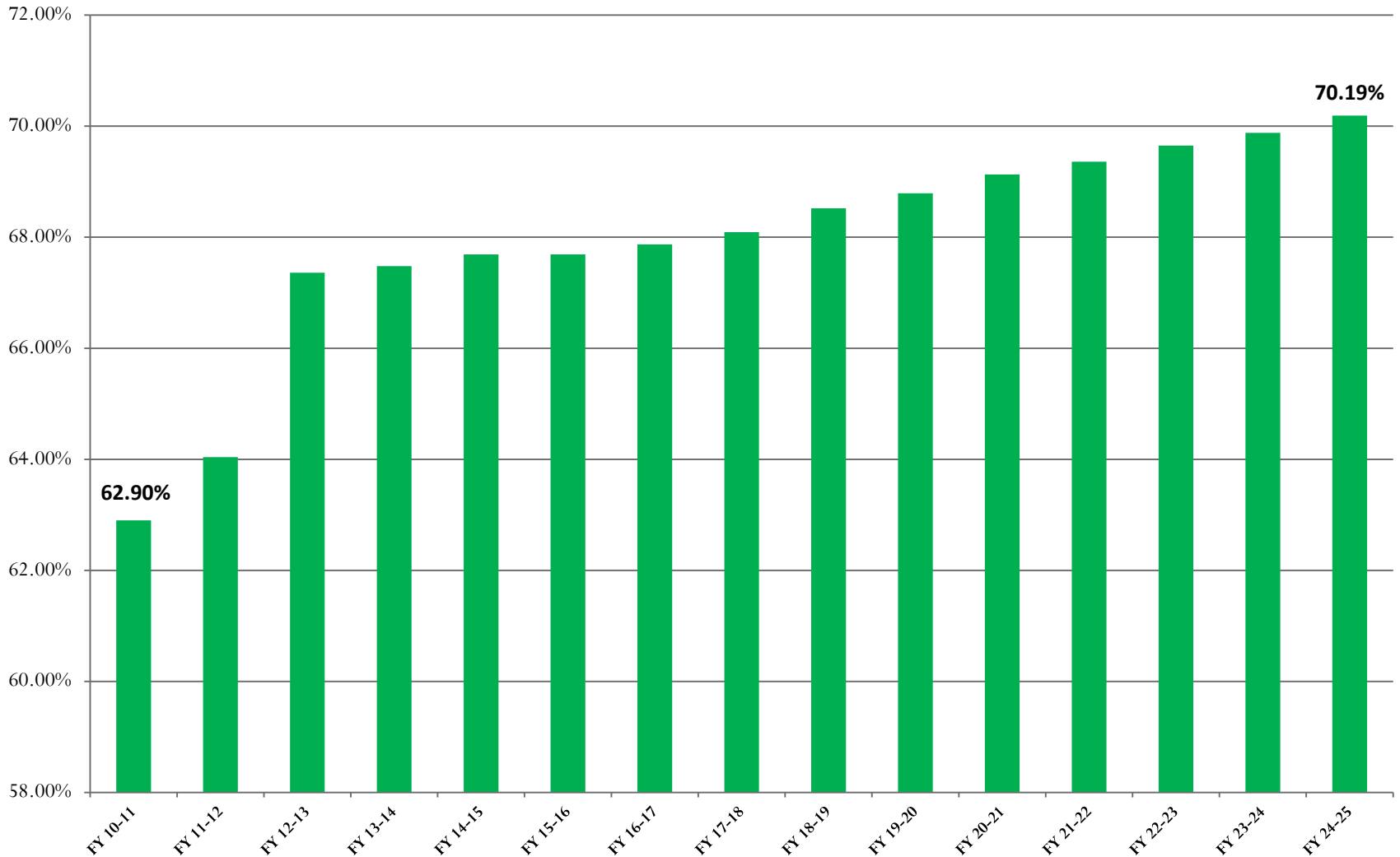


K-12 Local and State Shares: The Problem Illustrated



The State Share of School Finance will Continue to Grow

Forecast State Share with Levy Freeze



A Full Departmental Forecast of CDE Adds Slightly to K-12 Funding Costs

CDE General and State Education Fund Forecast

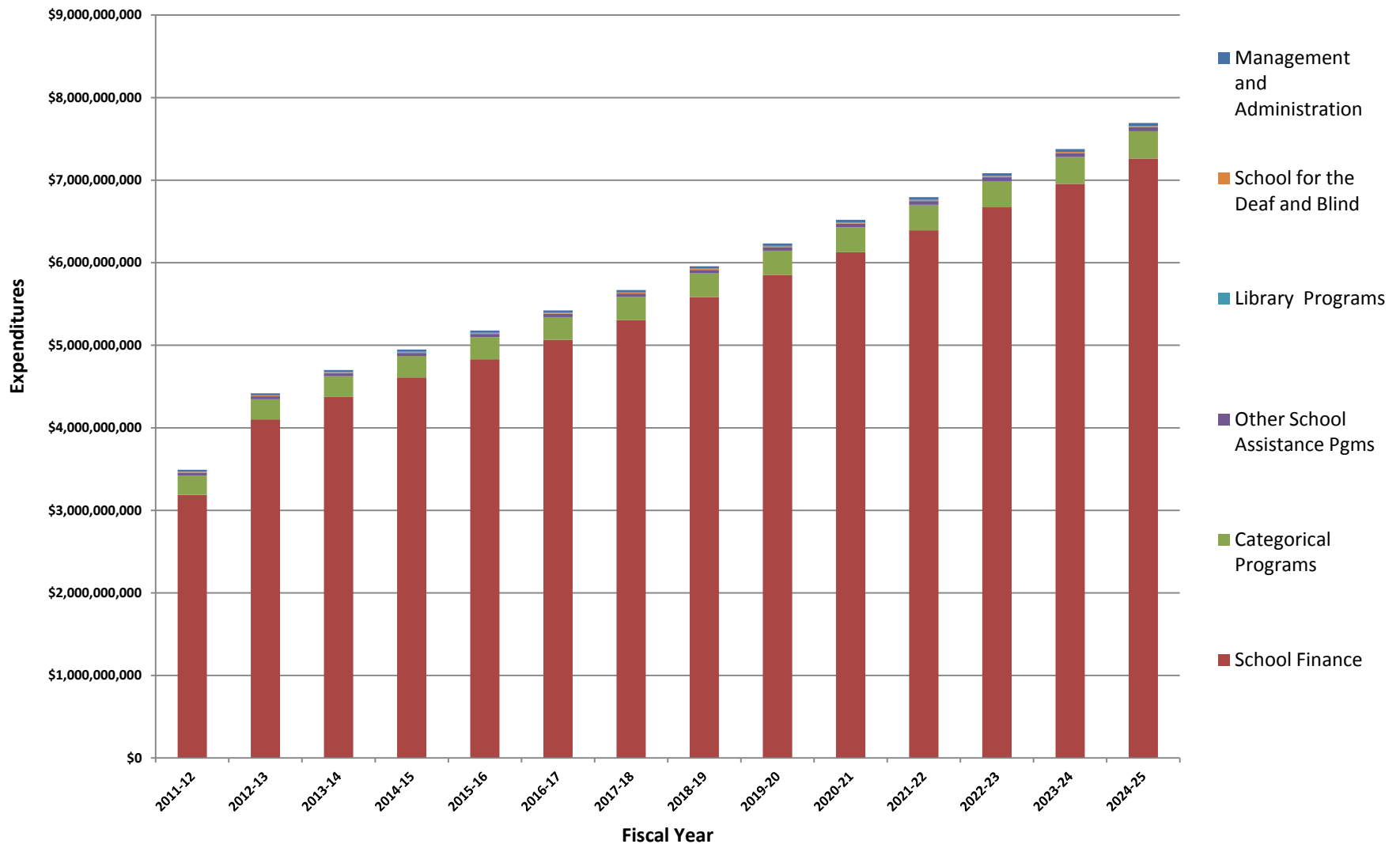


Illustration: Can the Structural Imbalance be Addressed with Cuts?

- Objectives of a Package of Cuts
 - Protect receipt of federal funds
 - Health Care Policy and Financing
 - Human Services
 - Fund the constitutionally created offices within the executive branch as well as the other 2 branches
 - Attorney General
 - Governor
 - State Treasurer
 - Fund the Department of Corrections

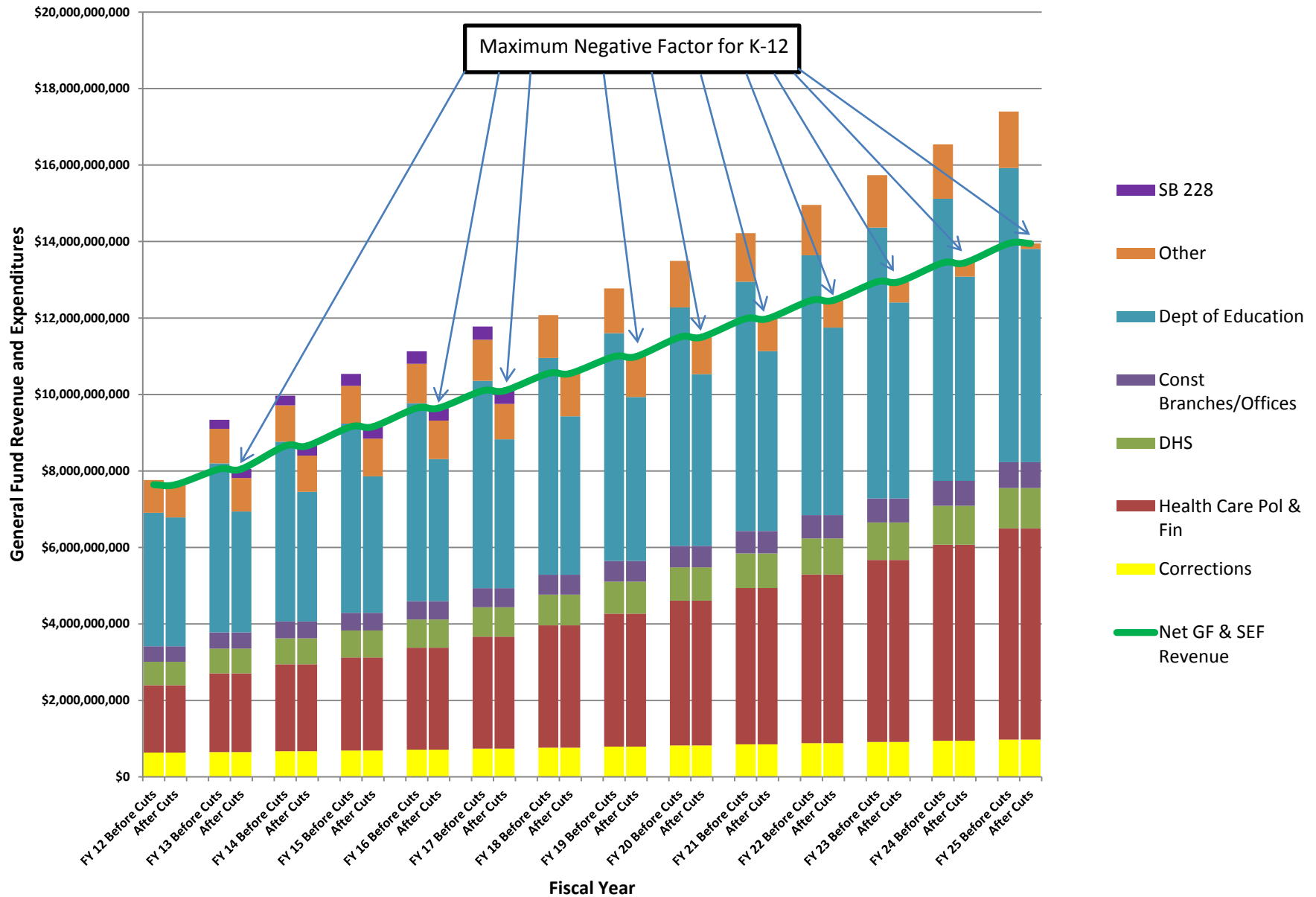
Illustration: A Cut Scenario

- Although K-12 per pupil base funding is protected by Amendment 23, it is thought that formula “factors” can be cut.
- Factors add about 25% to adjust for variances among districts in:
 - Enrollment size
 - Cost of living
 - Proportion of at-risk students
- Although 25% is added by the factors, only about 20% can be cut without affecting the per pupil base of some districts

Illustration: Cut Methodology

- Absorb first round of cuts by cutting up to the maximum in K-12
- Once K-12 cuts are maximized, cut the remaining 10 departments to balance the budget (programs in parentheses are the largest funded by the General Fund within each department)
 - Agriculture (Agricultural Services Division)
 - Higher education (College Opportunity Fund)
 - Local Affairs (Divisions of Local Government and Housing)
 - Military and Veterans Affairs (maintenance and utility costs for 15 armories)
 - Natural Resources (Division of Water Resources)
 - Personnel and Administration (Division of Accounts and Control)
 - Public Health and Environment (Prevention and Disease Control and Epidemiology Divisions)
 - Public Safety (Division of Criminal Justice, CBI, Colorado State Patrol)
 - Regulatory Agencies (Civil Rights Division)
 - Revenue (Taxation Business Group)

This is How Such a Package of Cuts Would Look



Distribution of “Other”

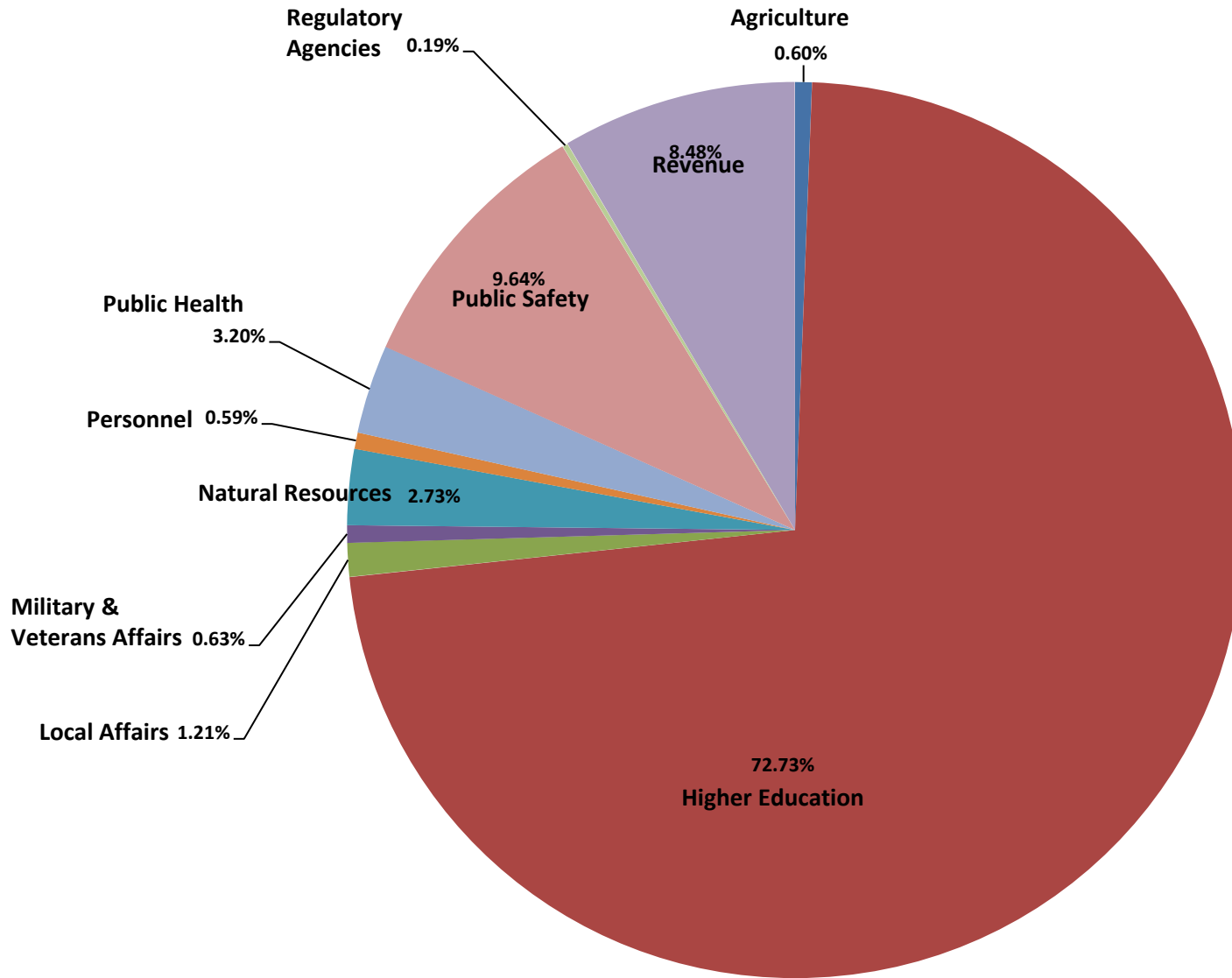


Illustration: Addressing the Structural Imbalance with Revenue

- Objectives of a package
 - Revenue sources that grow in step with future spending pressures (adequacy)
 - Revenues produced sufficient to fill the gap (capacity)
 - Revenue sources that reflect the structure of the economy (efficiency)
 - Revenue sources that are balanced
 - A balanced package would contain a mix of sources in which the strengths of each compensate for the weakness of others
 - Mitigate volatility
 - Address structural issues
 - Maintain or enhance the fairness of the tax system
 - Competitive with other states

Options for Addressing the Imbalance with Revenue

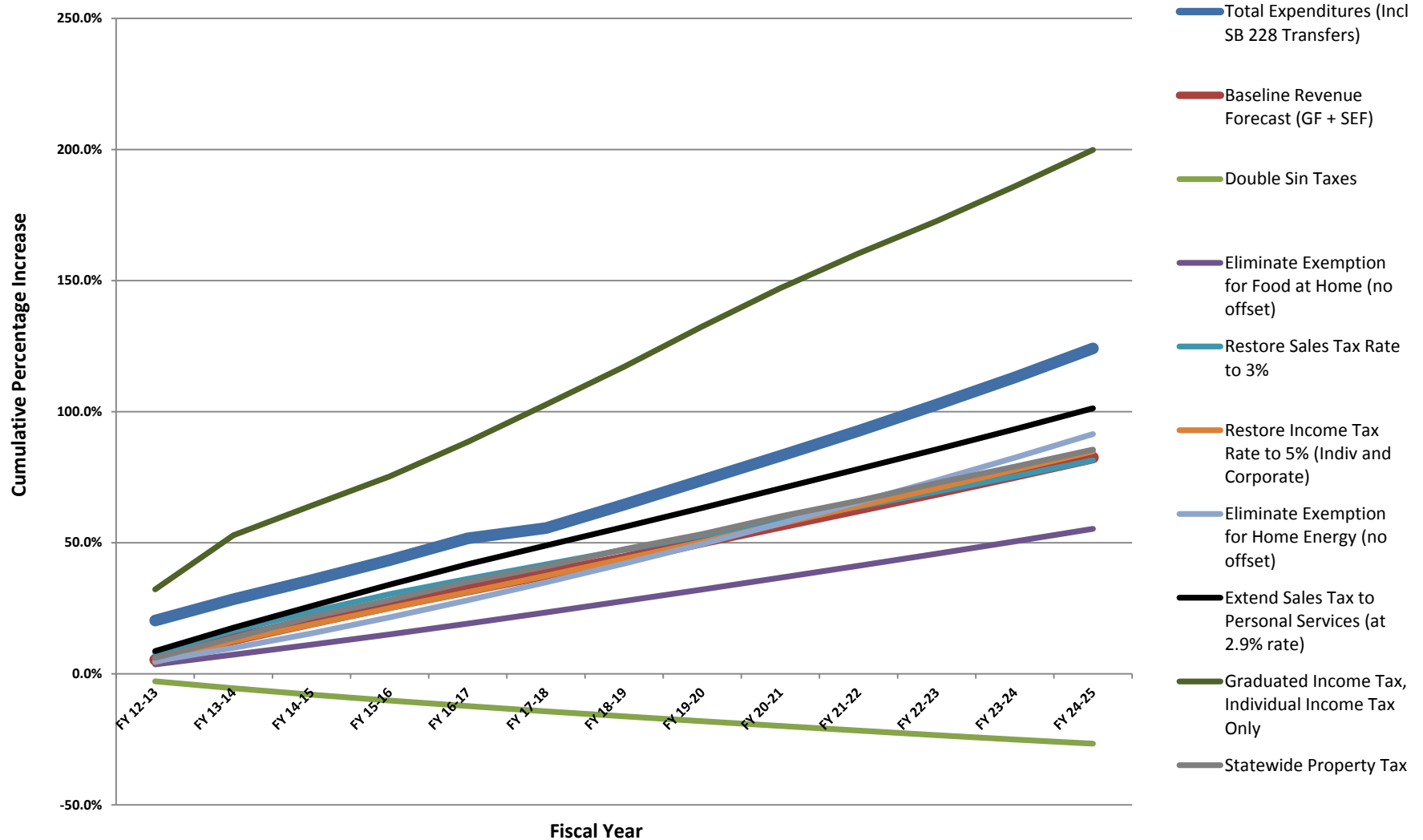
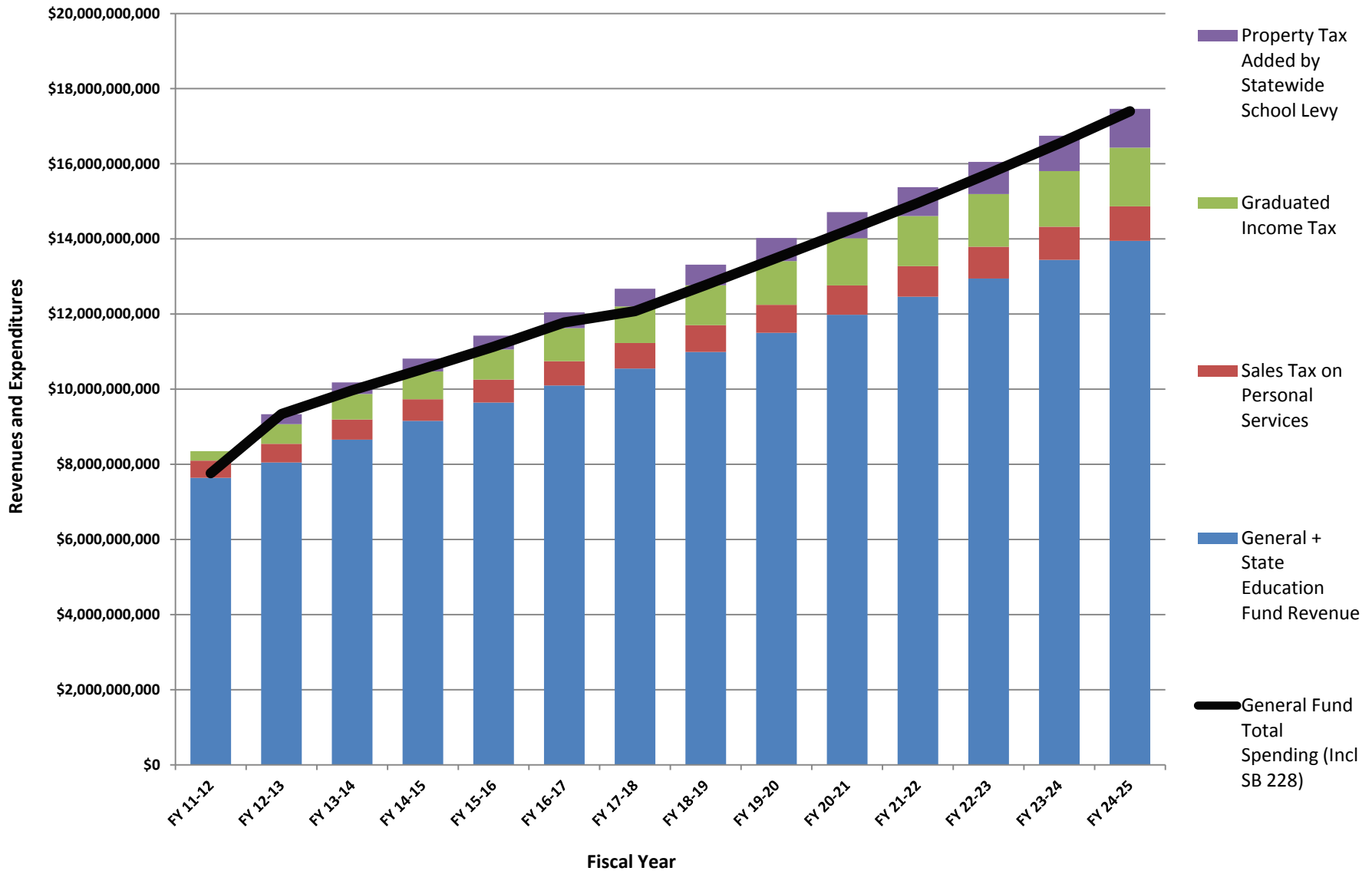


Illustration: Revenue Methodology

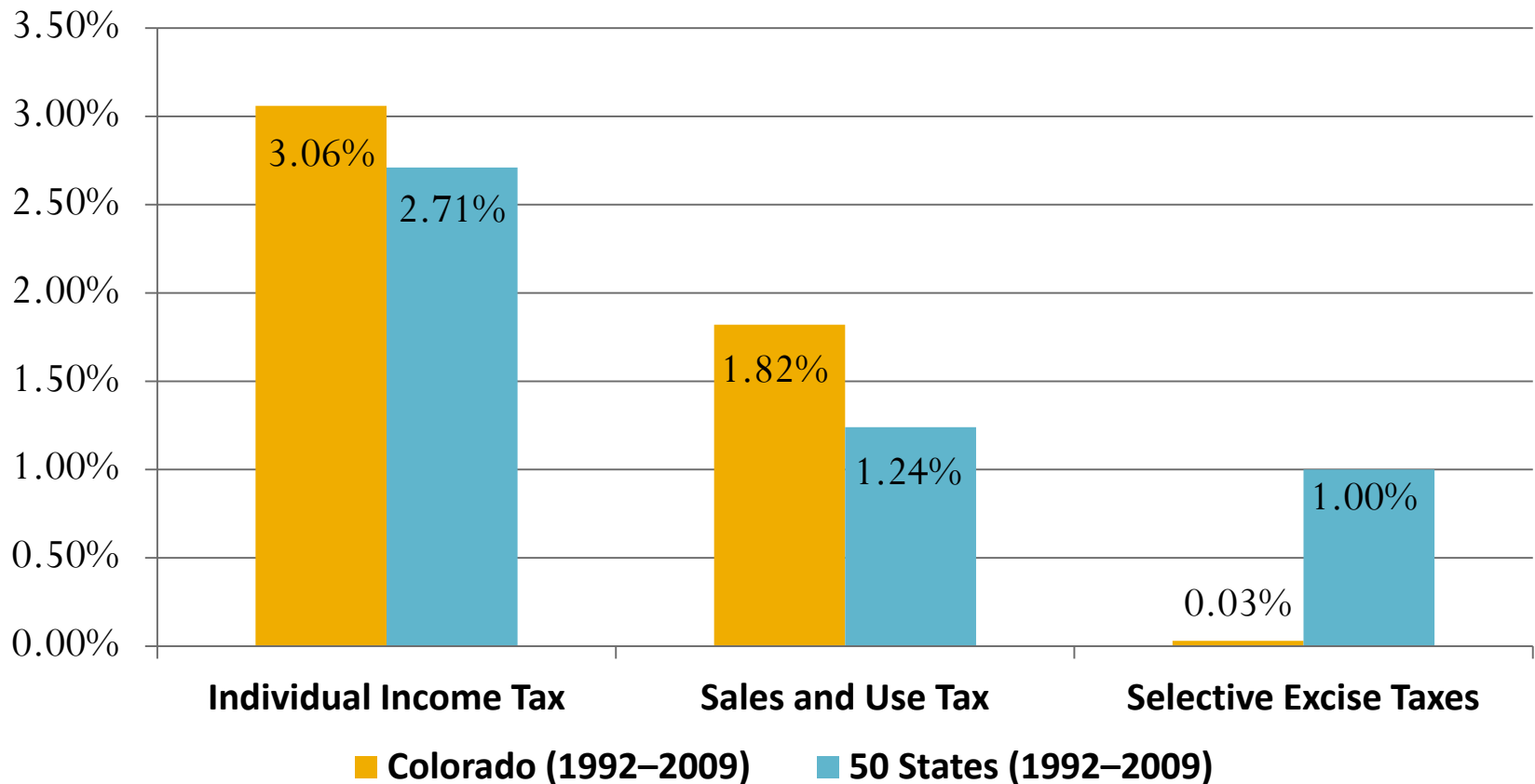
- Elements of a Package
 - Add personal services to the sales tax base
 - Levy property taxes for schools with a statewide mill levy
 - Phase statewide levy in for full implementation by FY 2024-25
 - Reduce state share from 63.2% to 60% over the phase-in period
 - Restore four graduated income tax brackets
 - Index the brackets to prevent “bracket creep”
 - Tax first \$50,000 of income (\$0 to \$50,000) at 4%
 - Tax next \$50,000 of income (\$50,000 to \$100,000) at 4.7%
 - Tax next \$100,000 of income (\$100,000 to \$200,000) at 5.4%
 - Tax income above \$200,000 at 6.1%

This is How Such a Package of Taxes Would Look



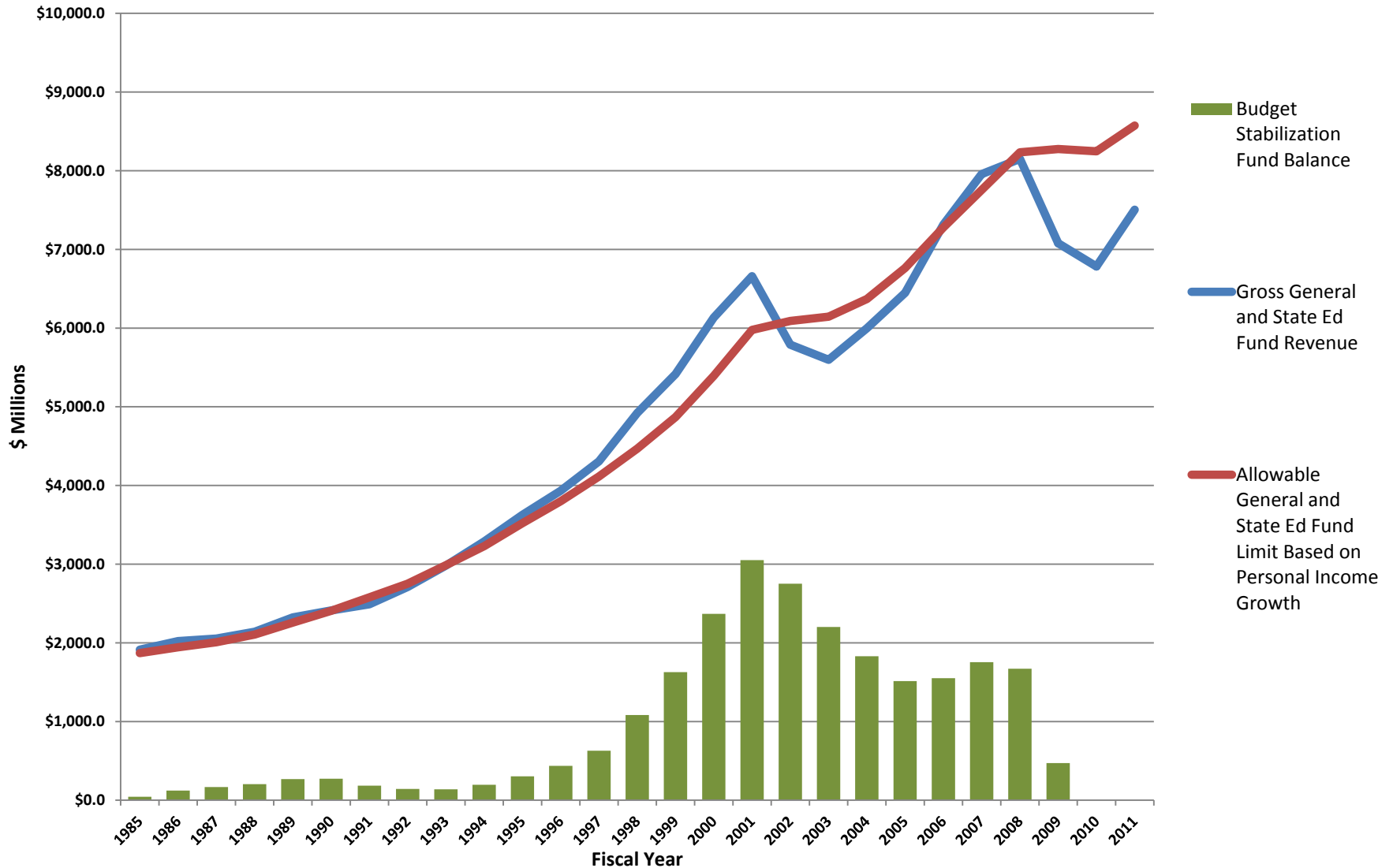
Volatility Remains a Concern

**Percent Increase in the Rate of Growth in the Revenue
Source that Results from a 1% Change in the Rate of Growth
of Personal Income**



Keeping the Wolf From the Door

Illustration: General Fund Spending Rule Based on Personal Income Growth and Budget Stabilization Fund



Minding the Store

- Forecasts are only as good as current assumptions and policies
 - Long term forecasting should be done routinely
 - Analyze policy changes for long term impact
- We agree with the GFOA recommendations
 - Financial capacity and long-term service objectives should be aligned
 - Longer term horizon - 10 years
 - Use revenue and expenditure forecasts, debt positions and monitoring mechanisms such as a scorecard of key indicators of financial health
 - Elected officials and the public should be able to easily grasp the government's long-term financial prospects and the strategies in place for achieving financial balance.

Thank You!

In addition to the direct support from the University of Denver, the following foundations supported this work

- Boettcher Foundation
- Bonfils-Stanton Foundation
- Colorado Health Foundation
- Colorado Trust
- El Pomar Foundation
- Gates Family Foundation
- Kaiser Permanente
- Piton Foundation
- Rose Community Foundation