



## COLORADO FISCAL POLICY INSTITUTE

Justice and Economic Security for *all* Coloradans

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#### **STRONG GENERAL FUND GROWTH LEADS TO MORE MONEY FOR ROADS AND CAPITAL CONSTRUCTION**

The most recent Legislative Counsel revenue estimate predicts significant General Fund revenue growth in FY 2005-06 with most of that gain benefiting transportation. Chief Legislative Economist Mike Mauer presented the June 2006 quarterly revenue figures to the Joint Budget Committee on Tuesday June 20.<sup>1</sup> Mauer's estimates include more moderate increases for all periods through Fiscal Year 2010-11.

The additional revenue will be kept and used by the state because voters approved Referendum C in November 2005 that sets aside for 5 years the inflation plus population revenue limit contained in the TABOR amendment. The 2005 voter bluebook estimated that the state could keep and use about \$3.743 billion over the five years, the June estimates now predicts that number to rise to \$4.885 billion.

The most significant change in revenue occurs in FY 2005-06. The additional revenue will mean, without legislative action in a special legislative session, the HUTF will receive a FY 2005-06 general fund transfer of \$256.7 million. This estimate is \$97 million higher than was expected when the legislature recessed in May. State capital construction will benefit by \$128.3 million from FY 2005-06 transfers, this is up \$48.5 million from the March estimate.

The increase in the revenue estimates do not significantly increase the amount of money available for any spending that is not capital or transportation. FY 2006-07 spending for general fund operating could increase \$6.3 million. The statutory 6% limit on general fund spending means that the benefits of the growing economy do not accrue to K-12 education, higher education or health care even with passage of Referendum C.

#### General Fund

The FY05-06 General Fund (GF) is now anticipated to receive \$6,934.9 million which includes \$1,016.9 million in General Fund Exempt money (funds that would have been refunded without the passage of Referendum C in November). Just three months ago, Leg. Council was predicting \$6,769.2 million. The increase of \$165.7 million will all go toward non-general fund uses, as the State's budget is already at the maximum allowable appropriations under the 6% spending limit.

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<sup>1</sup> See "Focus Colorado: Economic and Revenue Forecast, 2006-2011":  
[http://www.state.co.us/gov\\_dir/leg\\_dir/lcsstaff/lcs/focus/2006/06Forecast0620.pdf](http://www.state.co.us/gov_dir/leg_dir/lcsstaff/lcs/focus/2006/06Forecast0620.pdf)

Additionally, for the full forecast period, the GF revenue forecast is up by \$475.2 million. And over the next five years the increase in allowable GF spending changes little, for the same reason.

The main driver for the late change GF revenues is a spike in corporate income taxes. This is due to a one-time change in the federal tax code that allows U.S. companies to repatriate foreign earnings to the U.S. at a nominal tax rate. This is motivating companies to declare those earnings and pay these low rates. This translates into increased Colorado corporate income taxes, because the Colorado tax code utilizes federal adjusted gross income as the basis for assessing state taxes. Mr. Mauer cautioned that it is highly unlikely that this event will repeat itself.

In addition to the tax code change mentioned above, capital gains have risen due to a strong stock market (until recently), unemployment continues to fall (resulting in higher personal income taxes), and corporate profits are experiencing levels reminiscent of the peak of the 1990's economic boom. Stock returns can vary significantly, in fact, in the past few weeks major stock indexes have fallen, and some stock analysts expect a choppy market until at least this Fall. Mr. Mauer reported that in early 2006, total employment in Colorado finally reached the peak level just prior to the 2000 recession.

### Cash Funds

The major Cash Funds (CF) in the state budget are Transportation-related (fuel tax and auto and driver registration), Unemployment Insurance (UI) premiums, Severance Tax, and Limited Gaming Fund revenues.

*Transportation CF revenues* are in a relatively flat trend, and are expected to continue in this mode, for a number of reasons. The fuel tax is a per-gallon charge (as opposed to ad valorem which would be a percentage of gas sales). People are replacing their larger vehicles with smaller, more fuel-efficient ones, and no doubt responding to higher fuel prices by engaging in fuel-saving driving habits. This concerns legislative and executive branch leaders because the cost to maintain the transportation system in Colorado has not fallen with the reduced revenue base, and the state still has a backlog of projects in the trillions of dollars.

*Unemployment insurance revenues*, with a decrease of 1.3%, turned a corner this year, after experiencing increases of 58.5% and 36.1% over the previous two years. UI premium revenues, paid by employers, generally lag the real economy by about two years because higher premium rates and the solvency tax kick in when the fund balance falls. The reverse is true when the fund grows again. Benefits paid out in FY 04-05 were \$333.2 million, compared with three straight years of annual benefits at around \$500 million per year. This delayed counter-cyclical revenue effect generally wreaks havoc with the state budget under TABOR, which at present includes UI revenue in its base. During the 5-year time-out under Ref. C, this problem is suspended; however, beginning in the 6<sup>th</sup> year, it will return. Essentially, because UI is part of the TABOR base, and TABOR refunds are paid from the General Fund, any rise in UI revenues during poor economic times exacerbates the already falling GF that occurs when the economy falls. The GF is heavily dependant upon two cyclical revenue sources, income and sales taxes.

*Severance taxes* are experiencing a 52.5% increase this fiscal year due to the higher oil and gas prices and the increased production activity that these higher prices induce. Mr. Mauer reported that the levels of natural gas supply now in storage is now quite robust (50% higher than the average over the past 5 years). This over-supply condition may lead to a fall-off in natural gas prices this year and beyond, and thus affect severance tax revenue.

The story on *Gaming revenues* is surprising. The opening of the new Central City Parkway actually resulted in a slowing of gaming revenues. Central City has smaller gaming establishments

than its chief rival Black Hawk. This smaller scale, combined with the improved access to Central City, has meant that overall gaming receipts and thus taxes have weakened.

### HUTF and Capital Transfers

General Fund revenues received by fiscal year-end that are in excess of current year appropriations automatically transfer into the Highway Users Tax Fund (HUTF) and capital funds in a ratio of 2/3 – 1/3, respectively. The transfers occur in the early days of the next fiscal year, so they register in FY 06-07 on Leg. Council's General Fund Overview (see Table 1 of "Focus Colorado," lines 14 and 15) . Just since the March revenue forecast, these amounts have risen significantly. The transfer to HUTF goes from \$159.7 million, to \$256.7 million, an increase of \$97 million. The transfer to capital construction increases from \$79.8 million to \$128.3 million. While the June 2006 GF Overview shows no money in these lines beyond FY 06-07, this is somewhat misleading because in a growing economy it is likely that by fiscal year-end in subsequent years, the state will likely face the same scenario. The Joint Budget Committee typically uses the March revenue forecast from Leg. Council to balance the budget, and has historically made efforts to minimize the size of these automatic transfers in the budget-making process (for instance by appropriating such amounts for specific non-operating uses). But it can be concluded that as the economy continues to rebound under the 5-year time-out of Ref. C, the biggest and perhaps unexpected winners will be highways and capital projects.

Jim Zelenski  
Senior Fiscal Policy Analyst  
303-573-5669 ext. 304  
jzelenski@cclponline.org