

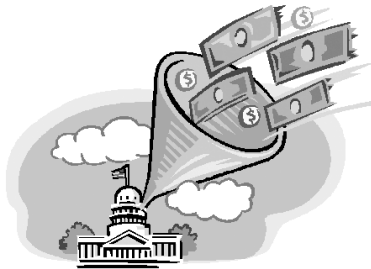
The TABOR Amendment

Coloradans like voting on tax increases, but did we get more than we bargained for?

Of the many pieces that make up the state's fiscal puzzle, the Taxpayer's Bill of Rights, commonly referred to as the TABOR Amendment, is the most complex and far-reaching. Praised, vilified and misunderstood, it has dominated the state's fiscal landscape since it was enacted 10 years ago. The purpose of the amendment was and is straightforward – to limit the growth of government and give voters the opportunity to approve tax increases in Colorado. Most would agree that the amendment has largely met these goals. TABOR, however, is about much more than simply allowing taxpayers to vote on tax increases; it represents the strictest taxing and spending diet that any state has ever experienced. With the current economic downturn, people are beginning to raise questions about how this diet will impact Colorado's future. The TABOR Amendment affects Colorado in many ways beyond voting on tax increases, but the following three are the most important:

1. TABOR itself is a revenue limit, not a spending limit –

Most limits on state government growth are true spending limitations. TABOR is very different in that it limits the total amount the state can accept as revenue. TABOR limits the amount of revenue Colorado government can keep from almost any revenue source including income tax, sales tax, college tuition – you name it. Year-to-year increases in the tax revenue Colorado collects cannot exceed the rates of inflation and population growth combined. This amount is called the TABOR revenue ceiling or TABOR limit. Any amount Colorado takes in beyond this revenue ceiling must be refunded to taxpayers unless they vote to let the state keep the excess.



Importantly, the population-plus-inflation formula is always applied to the state's actual revenues or the allowable revenue limit, whichever is lower, from the *immediately prior* year. When there is

Why population plus inflation? The Colorado revenue limit is not based upon historic economic data or the business cycles of our state. Colorado's revenue formula is a relatively severe one. Other states have limits that are based upon measures of economic performance such as Gross State Product (GSP) or personal income growth. These limits prevent unfettered growth in state government while recognizing economic cycles.

a significant revenue shortfall, such as we have experienced in the recent recession, the revenue limits are "ratcheted" down for the following years. Even if there is a strong economic recovery, state spending is NOT allowed to step back up to pre-recession levels. In effect, a revenue ceiling limits both what the state spends to operate day-to-day as well as what the state sets aside for construction, emergency reserves or savings. The TABOR revenue ceiling also interacts with a previously enacted spending limitation on the General Fund called the Arveschoug-Bird limit.

The severity of the revenue ceiling was not apparent during the economic boom of the 1990s. The state was awash in revenue and taxpayers started seeing "TABOR surplus" checks arriving in the mail by 1998. The large TABOR surplus partly justified significant and permanent sales and income tax reductions, as well as a mandate from voters called Amendment 23 that effectively infused a portion of the surplus money into K-12 schools. These changes, combined with today's economic slowdown, equate to unprecedented reductions in state services, construction and maintenance spending.

2. The "ratchet effect" – TABOR limits the state to revenue taken in the year before plus an allowance for inflation and population growth. So what happens in the bad times when state revenue is down and we don't even reach the inflation-plus-population limit? The TABOR revenue ceiling for the upcoming year is based upon what revenue Colorado can take in or what it actually *did* take in – whichever is lower. When the economy springs back as it always does, Colorado is stuck with a revenue limit based on the worst revenue year. This is known as the "ratchet effect" because like a ratchet wrench it only allows movement in one direction – down.



The TABOR revenue limits were intended to permanently prevent state government from expanding existing services and programs without cutting somewhere else, except to adjust for a growing or shrinking population. In fact, given that more than 75% of the state budget is spent on salaries, and the fact that salaries usually grow faster than inflation, TABOR ensures that government must become more efficient each year to provide the same services. However, when a recession hits, demand for services actually increases. Nonetheless, services must be severely cut and those cuts become permanent due to the ratchet effect. And this isn't just a theory. The 15% revenue shortfall in 2002 will mean a permanent reduction in state services, now and in the future.

An Example: Say that state revenues were \$100 last year and that population grew 1% and inflation was 3%. In this case, the state would be allowed to keep \$104. (1% + 3% = 4%) But what if the economy is weak, revenues are down and the state only takes in \$90 in revenue? In that case, next year's revenue ceiling is \$94 even if the economy rebounds and the state generates \$104 without raising taxes. Under TABOR's ratchet effect, services and most capital projects that are suspended during a downturn cannot be restored even when the economy recovers.

3. The “weakening provision” – When TABOR passed in 1992, a spending limit called the Arveschoug-Bird Limit had just been passed by the legislature. TABOR didn't change this existing limit but it did demand that any “limits on...spending and debt may be weakened only by future voter approval.” In other words, TABOR locked the Arveschoug-Bird limit into the constitution and it can no longer be changed by the legislature, only by the voters. So while TABOR is actually a revenue limitation, it “constitutiona-lized” an entirely separate and conflicting spending limitation, further reducing state budget flexibility.

The reach of the weakening provision goes beyond the state's Arveschoug-Bird spending limit. Prior to TABOR, local governments could “float” their property tax rates to provide consistent revenue to the locality from year to year. TABOR's weakening provision considers floating the mill levy a tax increase to be voted on by the people. Because elections are expensive and local government does not want to create a TABOR surplus, it is cheaper and easier to simply lower the tax rate every year. And lost local property tax revenues that fund public schools must be made up for by increased state budget allocations, squeezing out other state services.

