



FOCUS COLORADO: ECONOMIC & REVENUE FORECAST, 2003-2008

**State of
Colorado**

**June
2003**

**COLORADO LEGISLATIVE COUNCIL
STAFF REPORT**

COLORADO LEGISLATIVE COUNCIL STAFF FORECASTS, 2003-2008

MAIN TABLE OF CONTENTS

	Page
EXECUTIVE SUMMARY.....	3
REVENUE AND ECONOMIC FORECAST.....	5

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EXECUTIVE SUMMARY

General Fund Revenue

- The estimate for General Fund revenue in FY 2002-03 was reduced by \$28.0 million. Most of the decrease is from the accrual process rather than a large departure from our cash forecast in March 2003. Additionally, \$7.7 million of the decrease is attributable to the impact of federal tax reductions.
- The economy will be somewhat weaker than previously anticipated for the next year. Combined with the continuing impact of federal tax reductions on Colorado tax receipts, we reduced the forecast of General Fund revenue for FY 2003-04 by \$138.6 million. Revenue will increase by 4.1% in FY 2003-04, compared with our previous estimate of 6.1%.

General Fund Overview

- Use of remaining monies in the General Fund reserve will be sufficient to handle the additional revenue shortfall in FY 2002-03.
- However, the combined revenue shortfall for FY 2002-03 and FY 2003-04 leads to a General Fund budget that is out of balance by \$206.7 million in FY 2003-04.
- Use of the federal funds given to the states for their budget problems would be only a partial and temporary solution for the budget shortfall. Appropriations reductions would have to be eventually made to avoid chronic budget shortfalls.

Cash Funds

- Cash fund revenue subject to the TABOR revenue limit will increase by 1.6% in FY 2002-03. More robust growth rates beginning in FY 2003-04 will lead to a compound annual average growth rate of 5.5% during the forecast period.
- Growth after FY 2002-03 will largely be a function of increased fees imposed in light of budget shortfalls and automatic increases in the unemployment insurance tax rate and solvency taxes to keep the Unemployment Insurance Trust Fund solvent.
- Tuition revenue from the state's universities and colleges will increase by 13.0% in FY 2002-03, a 20-year high increase. Tuition revenue will increase by 9.5% while total higher education cash fund revenue will increase by 8.1% in FY 2003-04.
- Unemployment insurance taxes will increase 63.5% in FY 2003-04 and 43.1% in FY 2004-05. Tax rates will rise because benefit payments to the state's unemployed are depleting the fund balance below solvency levels.

The TABOR Revenue Limit

- Weak revenue growth will lead to the second consecutive absence of a TABOR surplus in FY 2002-03. Meanwhile, the population adjustment passed by the General Assembly will prevent a TABOR surplus from occurring in FY 2003-04.
- TABOR surpluses will reach a combined \$1.3 billion during the last four years of the forecast. The surpluses will be larger because of the many fee increases enacted during the 2003 legislative session. Additionally, the additional tax revenue generated to keep the Unemployment Insurance Trust Fund solvent will create larger TABOR surpluses. The TABOR surpluses will be refunded via the General Fund.

The National Economy

- While the national economy is currently weak, several factors are in place to generate more significant economic growth later this year. The factors include rising business, investor, and consumer confidence; lower energy prices; and, beneficial monetary and fiscal policy.
- Inflation-adjusted gross domestic product (**GDP**) will increase by 2.3% in 2003. However, the economy will expand at rates exceeding 3.5% in the third and fourth quarters. GDP will increase by 3.7% in 2004.
- The **unemployment rate** will peak later in 2003 and will average 6.0% this year. The rate will remain stubbornly high at 5.9% in 2004 before dropping to 5.4% in 2005. **Employment** growth will be nonexistent in 2003, before advancing by 1.2% in 2004 and 2.1% in 2005.

The Colorado Economy

- The state economy is very likely near the bottom of the downturn. However, the turnaround will be gradual.
- **Employment** will increase by a mere 0.1% in 2003, before advancing 2.0% next year. The **unemployment rate** will average 5.9% this year and 2.6% in 2004.
- Income indicators will be weak, but positive in 2003. After a 1.5% decline in 2002, **wage and salary income** will rise 1.9% in 2003. **Personal income** will increase 2.7% in 2003, following a 1.2% gain last year that ranked Colorado 49th in the country. Income gains will be stronger in 2004 as wages and salaries will increase 6.1% and personal income will advance 5.4%.
- A weak economy and goods deflation will keep the local **inflation rate** low at 2.0% in 2003. Inflation will be 2.8% in 2004.

Revenue and Economic Forecast

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REVENUE AND ECONOMIC FORECAST

TABLE OF CONTENTS

	Page
General Fund Revenue and Overview.....	9
Cash Fund Revenue Forecasts.....	19
Transportation-related Funds.....	21
Higher Education.....	24
Unemployment Insurance Trust Fund.....	28
Additional Cash Funds.....	31
Constitutional Revenue Limit.....	35
Overview of the Economy	
National Economy.....	39
Colorado Economy.....	43

General Fund Revenue and Overview

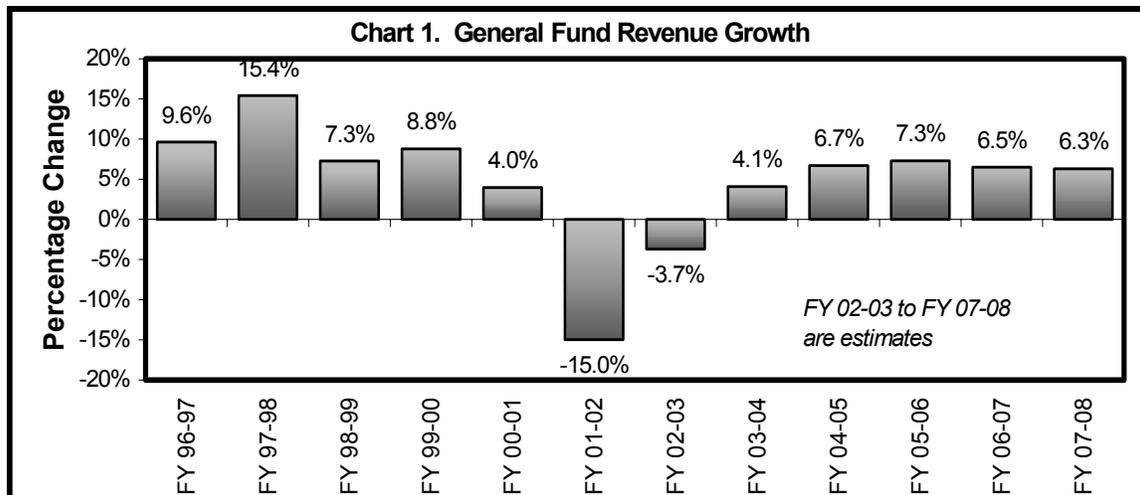
- The estimate for General Fund revenue in FY 2002-03 was reduced by \$28.0 million from the March 2003 forecast. Most of the decrease is from the accrual process because the revenue estimate for FY 2003-04 was reduced. \$7.7 million of the decrease is attributable to the impact of federal tax reductions on Colorado income taxes. Revenue will fall by 3.7% in FY 2002-03.
- The General Assembly put into place three mechanisms to cover revenue downturns from the March 2003 forecast. The first mechanism, a utilization of remaining monies in the General Fund reserve, will be sufficient to handle the additional shortfall for FY 2002-03.
- Based on a weaker economic forecast and the impacts from federal tax reductions, the forecast of General Fund revenue for FY 2003-04 was reduced by \$138.6 million. Revenues will increase by 4.1% in FY 2003-04, compared with our March estimate of 6.1%. Based on the revenue decrease, the General Fund budget is out of balance by \$206.7 million.
- General Fund revenue growth will be more robust beginning in FY 2004-05. However, the larger increases will not be sufficient to prevent budget shortfalls for that year and FY 2005-06. General Fund appropriations would need to be reduced by \$179.4 million and \$152.6 million for those two years in order to balance the budget, assuming that the budget was balanced in FY 2003-04 by reducing appropriations by \$206.7 million. While the recent federal funds received by Colorado could be used to help balance the budget, it would only delay when appropriations reductions need to be made.
- If the necessary reductions are made to balance the budget, the Senate Bill 97-1 diversion could resume on a partial basis for FY 2006-07. A full diversion could be made in FY 2007-08. In addition, \$7.6 million would be available in the excess General Fund reserve for transfer to the Highway Users Tax Fund and the Capital Construction Fund in FY 2007-08.

General Fund Revenue

This section presents the Legislative Council Staff outlook for General Fund revenues. Table 1 shows the forecast for FY 2002-03 through FY 2007-08.

Changes to the forecast. We reduced the March 2003 estimate of General Fund revenue for FY 2002-03 by \$28.0 million. The reduction is more a function of the impact of a weaker forecast for FY 2003-04 and how it affects tax accruals for FY 2002-03 than it is weaker receipts on a cash basis in the current year. We increased the cash forecast by \$31.1 million, largely based on realized investment gains by the state treasury. Revenue will decrease by 3.7% in the current fiscal year.

The recent Jobs and Growth Tax Relief Reconciliation Act of 2003 has three provisions that will affect the state's tax revenue. Colorado's individual and corporate taxes are linked to federal taxable income. Thus, when the federal government makes changes to definitions of income, exemptions, or deductions, the changes will affect Colorado's income taxes. A change to federal income tax rates does not have an impact on our taxes because they do not affect taxable income. The three provisions will reduce Colorado income tax revenue by an estimated \$90.0 million in FY 2002-03 through FY 2004-05. The revenue will be largely recaptured in years thereafter, however.



For FY 2003-04, we reduced the expected growth rate from 6.1% in March to 4.1%. Three factors contribute to the reduced revenue growth for FY 2003-04. First, because General Fund revenue was somewhat weaker for FY 2002-03, it will make the previous 6.1% estimate for FY 2003-04 an even larger, and increasingly unlikely, turnaround than previously expected. Second, we reduced the underlying economic forecast for 2003 and 2004. Third, federal tax law changes will have an impact on Colorado tax receipts.

The new tax law adopts an additional bonus depreciation deduction. Businesses may utilize a 50 percent depreciation deduction on qualified property compared with the current 30 percent allowance. The property must be acquired after May 5, 2003, and before January 1, 2005. This provision is the largest of the three provisions that will affect Colorado's tax revenue.

In what is known as section 179 expensing, the maximum amount that may be deducted under this provision is increased to \$100,000 from \$25,000 for tax years 2003 through 2005. Qualifying property under this provision is de-

**Table 1
June 2003 General Fund Revenue Estimates
(Dollars in millions)**

Category	Estimated FY 2001-02	Percent Change	Estimate FY 2002-03	Percent Change	Estimate FY 2003-04	Percent Change	Estimate FY 2004-05	Percent Change	Estimate FY 2005-06	Percent Change	Estimate FY 2006-07	Percent Change	Estimate FY 2007-08	Percent Change
Sales /A	\$1,755.6	-3.1	\$1,687.3	-3.9	\$1,744.3	3.4	\$1,831.4	5.0	\$1,920.9	4.9	\$2,035.8	6.0	\$2,153.9	5.8
TABOR Overfund	-28.6	-52.4	-19.9	-30.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Use /A	140.6	-10.9	127.3	-9.5	133.2	4.7	141.0	5.9	148.2	5.1	156.2	5.4	164.5	5.3
Cigarette	55.2	-5.0	53.5	-3.0	52.8	-1.4	51.4	-2.7	49.6	-3.4	48.4	-2.5	47.2	-2.5
Tobacco Products	10.3	4.5	10.3	0.0	11.1	7.5	11.6	4.6	12.1	4.2	12.7	5.1	13.4	5.0
Liquor	29.5	0.7	29.2	-1.1	30.0	2.9	30.8	2.6	31.6	2.6	32.4	2.6	33.2	2.4
TOTAL EXCISE	\$1,962.7	-2.2	\$1,887.7	-3.8	\$1,971.5	4.4	\$2,066.3	4.8	\$2,162.5	4.7	\$2,285.5	5.7	\$2,412.1	5.5
Net Individual Income	\$3,345.2	-16.7	\$3,095.1	-7.5	\$3,382.2	9.3	\$3,627.6	7.3	\$3,923.7	8.2	\$4,200.7	7.1	\$4,494.2	7.0
Net Corporate Income	178.0	-46.0	188.1	5.7	176.6	-6.1	241.2	36.6	308.8	28.0	330.4	7.0	346.6	4.9
TOTAL INCOME TAXES	\$3,523.2	-19.0	\$3,283.2	-6.8	\$3,558.8	8.4	\$3,868.7	8.7	\$4,232.4	9.4	\$4,531.1	7.1	\$4,840.8	6.8
Less: Portion directed to the State Education Fund /B	-272.9	66.1	-188.4	-31.0	-267.9	42.2	-290.8	8.6	-317.7	9.2	-339.8	7.0	-362.7	6.7
INCOME TAXES TO GENERAL FUND	\$3,250.3	-22.3	\$3,094.8	-4.8	\$3,290.9	6.3	\$3,578.0	8.7	\$3,914.8	9.4	\$4,191.2	7.1	\$4,478.1	6.8
Estate	\$72.5	-12.2	\$54.5	-24.8	\$32.0	-41.3	\$17.0	-46.9	\$1.4	-91.6	\$0.0	-100.0	\$0.0	NA
Insurance	154.6	8.9	173.6	12.3	182.7	5.3	190.1	4.0	202.3	6.4	215.2	6.4	228.0	5.9
Pari-Mutuel	5.7	-5.8	4.6	-19.2	6.2	33.6	6.2	0.0	6.2	0.0	6.1	-1.6	6.0	-1.6
Interest Income	25.3	-44.0	44.7	76.6	15.7	-64.9	16.8	7.0	17.6	4.8	18.9	7.4	20.5	8.5
Court Receipts	23.3	4.4	25.7	10.4	26.5	3.0	27.2	2.8	28.0	2.8	28.7	2.7	29.4	2.5
Gaming /C	34.1	8.5	37.1	8.9	38.9	4.8	38.9	0.0	41.2	6.1	44.1	6.8	46.9	6.3
Medicaid (Intergovt. Transfer)	11.2	NA	15.6	39.6	0.0	NA								
Other Income	31.9	-4.4	28.3	-11.4	22.4	-20.9	23.2	3.8	24.1	3.8	25.0	3.7	25.9	3.5
TOTAL OTHER	\$358.6	-1.2	\$384.1	7.1	\$324.4	-15.6	\$319.4	-1.5	\$320.9	0.5	\$338.0	5.3	\$356.7	5.5
GROSS GENERAL FUND	\$5,571.6	-15.0	\$5,366.7	-3.7	\$5,586.7	4.1	\$5,963.7	6.7	\$6,398.1	7.3	\$6,814.8	6.5	\$7,246.9	6.3
REBATES & EXPENDITURES:														
Cigarette Rebate	\$15.9	-3.0	\$15.4	-3.0	\$15.2	-1.4	\$14.8	-2.7	\$14.3	-3.4	\$13.9	-2.5	\$13.6	-2.5
Old-Age Pension Fund	72.0	13.9	76.0	5.6	79.6	4.8	84.2	5.8	89.4	6.1	95.1	6.4	102.1	7.3
Aged Property Tax & Heating Credit	23.6	40.5	14.9	-36.8	17.0	14.1	16.9	-0.8	16.6	-1.4	16.9	1.8	16.8	-0.7
Fire/Police Pensions	28.9	0.7	29.1	0.6	3.8	-86.9	3.8	0.0	29.1	665.8	29.1	0.0	29.1	0.0
TOTAL REBATES & EXPENDITURES	\$140.4	9.5	\$135.4	-3.5	\$115.6	-14.6	\$119.7	3.5	\$149.4	24.8	\$155.1	3.8	\$161.6	4.2

Totals may not sum due to rounding.

NA: Not Applicable.

/A Sales and use taxes diverted to the Highway Users Tax Fund can be found in Table 2.

/B In November 2000, Colorado voters approved Amendment 23 that deposits an amount equal to 0.33 percent of Colorado taxable income into the State Education Fund. These revenues are exempt from the TABOR revenue limit.

/C Includes only the amount credited to the General Fund.

financed as depreciable tangible personal property that is purchased for use in the active conduct of a trade or business. The provision is intended for small businesses with small annual investments. Under previous law, the \$25,000 maximum expensing was reduced by the amount by which the cost of qualifying property placed in service during the taxable year exceeded \$200,000. The new law increases the latter threshold to \$400,000. Both the new \$100,000 and \$400,000 thresholds will be indexed for inflation beginning in tax year 2004.

A third provision relating to the federal alternative minimum tax (AMT) will reduce Colorado tax revenue minimally. Colorado has had an AMT for individual taxpayers since 1987 that is based on the amount of federal alternative minimum taxable income. The new federal tax law increases the AMT exemption amount by \$4,500 for single taxpayers and \$9,000 for married taxpayers.

“It is likely that some previous capital gains realizations will be unlocked and some short-term unquantifiable revenue gains will occur.”

It should be noted that a new federal law that accelerates the marriage penalty relief via an increased standard deduction amount will not affect Colorado revenue. The state passed an increased standard deduction amount in 1999 (House Bill 99-1003) that was first effective for tax year 2000. Provisions in the new federal tax law that reduce federal taxes on dividend and capital gains income through lower tax rates will not directly affect Colorado tax revenue. However, it is likely that some previous capital gains realizations will be unlocked and some short-term unquantifiable revenue gains will occur. Similarly, the reduced federal taxes on dividend income may induce additional dividends that would increase Colorado tax revenue.

The impacts of federal tax cuts are somewhat offset by actions taken by the General Assembly during the recent legislative session that increase revenue. These actions will increase General Fund revenue by an estimated \$31.9 million in FY 2003-04 and \$35.9 million in FY 2004-05. The 3 1/3% discount currently given to businesses to offset their costs of collecting sales, use, tobacco, and cigarette taxes was reduced by one percentage point for two years only in *Senate Bill 03-317*. The state will collect an additional \$18.2 million and \$19.1 million in FY 2003-04 and FY 2004-05, respectively. *Senate Bill 03-107* permits additional simulcast races at the state's dog racing tracks. Wagering on the additional races will generate \$1.3 million annually.

Senate Bill 03-300 imposes a monthly management fee on state moneys invested by the State Treasurer. The bill directs the State Treasurer to credit the fee to the General Fund. The fee is expected to generate \$3.5 million annually. *House Bill 03-1382* reduces the interest rate that the state pays on tax refunds and is expected to generate \$1.4 million additional revenue for the state's income, sales, and use taxes in FY 2003-04. The additional revenue will increase to \$4.5 million in FY 2004-05 and thereafter. *House Bill 03-1274* permits low-interest loans to be made to school districts. The loans were previously interest free loans. The state will earn an estimated \$3.0 million annually on the loans. *Senate Bill 03-271* provides for increased surcharges on traffic and motor vehicle violations and directs that the money goes to the General Fund. Revenue will increase by \$4.5 million on an ongoing basis.

“Revenue to the General Fund this year will be nearly \$1.2 billion below the peak level of \$6.55 billion in FY 2000-01.”

Revenue to the General Fund this year will be nearly \$1.2 billion below the peak level of

\$6.55 billion in FY 2000-01. Revenue will not surpass this peak level until FY 2006-07.

Major categories of the revenue forecast. We reduced the forecast for most revenue sources. The state **sales tax** has not yet shown any signs of a recovery. In fact, tax receipts have become even weaker in recent months. However, we believe that the additional weakness was caused by one-time factors. A historic snowstorm and the onset of the brief war with Iraq in March caused tax receipts in April to plummet by 8.6% compared with the previous year. Receipts for February economic activity declined by 5.1% and the looming war was a probable cause. The tax receipts for April activity were somewhat better.

“Tourism activity will be better in 2003 and will provide the initial impetus for stronger sales tax receipts in FY 2003-04.”

Sales taxes will decline by 3.9% in FY 2002-03. We expect that an economic recovery will gradually take hold in Colorado. Tourism activity will be better in 2003 and will provide the initial impetus for stronger sales tax receipts in FY 2003-04. A slight deflationary trend for some goods will constrain growth. Sales taxes will increase by 3.4% in FY 2003-04. Without the reduced discount for retailers and other businesses, sales taxes would have increased by 2.5%. In the March 2003 forecast, we estimated that sales tax receipts would increase by 4.8%.

The state **use tax** collections have been weak for two years, coinciding with the decline in business investment. After declining by 10.9% in FY 2001-02 (influenced by the tax rate reduction in January 2001), use tax receipts will drop by 9.5% in FY 2002-03. A rebound in business investment and confidence will lead to a 4.7% increase in use taxes in FY 2003-04. The growth rate is 0.4 per-

centage points higher because of the reduced discount on the retailer use tax. Growth will be in the five to six percent range through the remainder of the forecast period.

“Cigarette tax collections have declined for three consecutive years and will continue to decline throughout the forecast period.”

Cigarette tax collections have declined for three consecutive years and will continue to decline throughout the forecast period. Fewer people are smoking because of health concerns. Additionally, consistent price increases dissuade many from smoking as much. During the past three years, cigarette taxes declined at a 2.7% annual rate. Our baseline forecast is for a 2.5% annual decline. However, the actual growth rates for FY 2003-04 through FY 2005-06 are influenced by the reduced vendor allowance per Senate Bill 03-317.

Tobacco tax collections increased at a slower rate in FY 2001-02, relative to previous years. They will be flat in FY 2002-03, influenced by a negative tax accrual. Collections will be stronger in the later years of the forecast.

Liquor consumption declined in FY 2002-03 because of the slow economy. Consequently, **liquor taxes** are expected to decline 1.1%. They will increase again during the rest of the forecast period.

“Individual income taxes will decline by 7.4%, or \$246.6 million this year, following a precipitous 16.7% decline in FY 2002-02.”

Individual income taxes will decline by 7.5%, or \$246.6 million this year, following a precipitous 16.7% decline in FY 2001-02. Several factors are contributing to the declines of the past two years. Taxes from nonwage

income sources such as capital gains and interest earnings are substantially lower. Preliminary data from the Internal Revenue Service indicated that capital gains declared nationwide on federal income tax returns dropped 44.5% for tax year 2001. While data is not available for tax year 2002, we believe that capital gains realizations declined again in 2002 coinciding with the bear market decline. This was evidenced by an estimated 4.9% decline in estimated payments and a 22.1% decline in cash settlements on income tax returns. To the extent that many Colorado stockholders took realized losses on their portfolios, the losses reduce taxable income on income tax returns. These losses will carry forward for several years as taxpayers are limited to deducting only a \$3,000 capital loss each year.

Wage and salary income contracted by 1.5% in Colorado in 2002. Based on withholding tax receipts, wage growth likely is in negative territory through the first part of 2003 as well. Because of the weak labor market, workers are no longer able to bid up their wages as they did in the boom years of the late 1990s. Similarly, bonus and stock option earnings have largely disappeared. Employers are trying to hold the line on wage increases to keep costs under control. Employers' rising costs for benefits are also constraining their willingness to give wage and salary increases.

Finally, the accrual estimates for individual income taxes will account for more than half of this year's decline. Estimates a year ago for current year refunds were underestimated. Because we expect that refunds will increase again in FY 2003-04, the accrual process will reduce revenue in FY 2002-03.

Receipts from individual income taxes will resume a growth path in FY 2003-04 after the two-year decline. Individual income taxes will increase 9.3% in FY 2003-04. However, this strong growth rate is not completely related to

the economy. The volatile pattern of accruals will lead to a small positive accrual. However, the expected \$13.6 million positive accrual for FY 2003-04 compares with the expected \$134.1 million negative accrual for FY 2002-03. The large swing in the accrual contributes to the 9.3% growth rate. By contrast, income taxes on a cash basis will increase by only 4.9% in FY 2003-04.

Individual income tax revenue will be affected by the federal tax cuts. We estimate that the cuts will reduce Colorado individual income taxes by \$23.5 million in FY 2003-04 and \$14.4 million in FY 2004-05.

Corporate income taxes declined by 46.0% in FY 2001-02. Corporate taxes appeared headed for another decline in the last forecast, but have since experienced a modest rebound. We anticipate that they will now increase by 5.7% this year. However, they will decline again in FY 2003-04 because of how the federal tax law changes affect corporate tax liability. We estimate that the new law will reduce corporate revenue by \$27.6 million next fiscal year.

“Insurance premium taxes will have the most robust growth for the state’s General Fund taxes in FY 2002-03, increasing 12.3%.”

Insurance premium taxes will have the most robust growth for the state's General Fund taxes in FY 2002-03, increasing 12.3%. They will increase by 5.3% in FY 2003-04. **Interest earnings** for the General Fund have suffered over the last two years because of declining revenue and appropriations that did not match the revenue decline. They declined by 44.0% in FY 2001-02. The interest earnings category includes investment earnings. The state treasury realized \$35.8 million in gains in mid-June as it sold investments to pay back the short-term borrowing throughout FY 2002-03. The investment gains are one time in nature.

Interest earnings in the General Fund will reach \$15.7 million in FY 2003-04 and will be boosted by two law changes.

Gaming revenue that accrues to the General Fund will total \$37.1 million in FY 2002-03, an 8.9% advance. Reduced appropriations from the gaming fund will boost the amount that spills into the General Fund. The forecast of revenue does not include the impact of Senate Bill 03-274. The additional revenue provided for in the legislation is included as a transfer of cash fund revenue to the General Fund. Modest increases in gaming activity will slow the growth rate of gaming revenue. We project that the General Fund portion of gaming taxes and fees will increase by 4.8% in FY 2003-04.

General Fund Overview

This section presents the General Fund overview after incorporating the revenue forecasts, the expected TABOR surpluses, and other expenditures from the General Fund. Table 2 presents the General Fund overview.

Because of the additional revenue decline, the General Assembly needed to take steps to balance the General Fund budget for FY 2002-03 and FY 2003-04. While the steps were sufficient to balance the budget for FY 2002-03, even more action will need to be taken to achieve a balanced budget for FY 2003-04.

“...even more action will need to be taken to achieve a balanced budget for FY 2003-04.”

We estimate that the year-end General Fund balance for FY 2002-03 will be \$61.4 million. In order to reach that point, the General Assembly took the following steps during the recent legislative session:

- reduced General Fund appropriations from \$5.950 billion to \$5.415 billion, a \$535 million reduction. Of this amount, \$166.4 million is one-time in nature and will need to be funded in FY 2003-04. General Fund appropriations went from a 5.26% increase as passed by the General Assembly a year ago to a 4.22% decrease after the supplementals.
- transferred \$349.6 million from cash funds to the General Fund.

These actions came on top of a transfer of \$219.0 million from cash funds to the General Fund at the beginning of the fiscal year. Based on the March 2003 revenue estimate, the General Assembly took the following steps for FY 2003-04:

- increased appropriations by 2.3% rather than the maximum allowable 6.0%;
- allowed for the transfer of \$38.4 million from cash funds;
- reduced the diversion of sales and use tax revenue to the Older Coloradans and Supplemental Old Age Pension Health and Medical Care cash funds;
- provided for enhancements to revenue as detailed in the General Fund revenue section;
- eliminated the senior homestead exemption for FY 2003-04 and the following two years;
- delayed again the scheduled reimbursement of the Controlled Maintenance Trust Fund (CMTF);
- eliminated for two years a payment for firemen and policemen pensions; and,

Table 2
June 2003 General Fund Overview
(Dollars in millions)

	Actual FY 2001-02	Estimate FY 2002-03	Estimate FY 2003-04	Estimate FY 2004-05	Estimate FY 2005-06	Estimate FY 2006-07	Estimate FY 2007-08
Beginning Reserve	\$469.3	\$137.6	\$97.2	\$213.3	\$219.3	\$226.3	\$239.9
Gross General Fund	5,571.6	5,366.7	5,586.7	5,963.7	6,398.1	6,814.8	7,246.9
Senate Bill 97-1 Diversion to the HUTF /A	****	0.0	0.0	0.0	0.0	-112.2	-240.1
Paybacks to Other Funds	536.3	-349.6	-10.0	0.0	0.0	0.0	-13.7
Transfers from Other Funds	****	568.6	38.4	-2.3	-2.8	-2.8	-2.8
Diversion of Sales Taxes to Other Funds	****	-3.0	0.0	-113.6	-341.5	-477.4	-394.7
TABOR Surplus Liability	253.4	0.0	0.0	0.0	0.0	0.0	0.0
Transfer from the Controlled Maintenance Trust Fund /D	\$6,830.6	\$5,720.3	\$5,710.1	\$6,061.2	\$6,273.2	\$6,448.7	\$6,835.5
Total Funds Available							
EXPENDITURES:							
Allowable General Fund Appropriations /B	\$5,643.0	\$5,414.5	\$5,538.4	\$5,641.6	\$5,791.1	\$5,978.1	\$6,337.9
Necessary Reductions to Balance Budget		\$0.0	-\$206.7	-\$179.4	-\$152.6		
Medicaid Overexpenditure	0.0	NE	NE	NE	NE	NE	NE
Rebates and Expenditures	140.4	135.4	115.6	119.7	149.4	155.1	161.6
Reimbursement for Senior Property Tax Cut	0.0	62.6	0.0	0.0	0.0	55.1	53.6
Capital and Prison Construction	****	10.6	9.5	101.8	100.7	0.6	0.5
Transfer for Highway Construction	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Transfer to the Controlled Maintenance Trust Fund /C	0.0	0.0	40.0	138.2	138.2	0.0	0.0
K-12 Settlement Funding Adds to GF Appropriation /B, D	10.0	0.0	0.0	20.0	20.0	20.0	20.0
TABOR Refund	927.2	0.0	NA	NA	NA	NA	NA
Accounting Adjustments	-27.6	NE	NE	NE	NE	NE	NE
Total Obligations	\$6,693.0	\$5,623.1	\$5,496.8	\$5,841.9	\$6,046.8	\$6,208.9	\$6,573.6
YEAR-END GENERAL FUND RESERVE:	\$137.6	\$97.2	\$213.3	\$219.3	\$226.3	\$239.9	\$261.9
STATUTORY RESERVE: 4.0% OF APPROPRIATIONS /E	0.0	97.2	213.3	219.3	226.3	239.9	254.3
GENERAL FUND EXCESS RESERVE	\$137.6	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$7.6
Funds in Excess Reserve to Highway Users Tax Fund	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$5.1
Funds in Excess Reserve to Capital Construction	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$2.5
RESERVE AS A % OF APPROPRIATIONS	2.4%	1.8%	4.0%	4.0%	4.0%	4.0%	4.1%
TABOR RESERVE REQUIREMENT:							
General & Cash Fund Emergency Reserve Requirement	\$232.6	\$227.5	\$242.8	\$257.6	\$268.6	\$281.5	\$295.9
Appropriations Growth /C	\$303.4	-\$238.5	-\$82.8	\$150.5	\$176.4	\$339.5	\$359.9
Appropriations Growth Rate /C	5.67%	-4.22%	-1.53%	2.82%	3.22%	6.00%	6.00%
Addendum: Amount Directed to State Education Fund	\$272.9	\$188.4	\$267.9	\$290.8	\$317.7	\$339.8	\$362.7

NE: Not Estimated.

Totals may not sum due to rounding.

**** The diversion of sales and use tax revenues (\$35.2 million) to the HUTF, the diversion (\$3.0 million) to the Older Americans Fund, and the transfer (\$83.3 million) to the Capital Construction Fund are contained in the General Fund appropriations amount.

/A 10.355% of sales and use taxes are diverted to the Highway Users Tax Fund when the full six percent General Fund appropriations limit can be attained. The amount was capped at \$35.2 million for FY 2001-02 and does not occur or is limited in some years thereafter due to insufficient General Fund revenue.

/B The amounts for the K-12 settlement funding attributable to Senate Bill 00-181 are also appropriations from the General Fund and should be added to the General Fund appropriations line to calculate total appropriations.

/C House Bill 01-1267 transferred the principal balance of the CMTF to the General Fund on July 1, 2001. HB 03-262 transfers \$138.2 million from the General Fund to the CMTF in FYs 2004-05 and 2005-06. SB 03-268 requires the transfer of \$40 million to the CMTF for a cash flow reserve.

/D The settlement requires that the General Fund have at least \$80 million in excess reserves for funding to take place. Because the General Assembly has funded the settlement in two budget years without reaching the \$80 million threshold, it has been included in this overview for all years except FY 2002-03 and FY 2003-04 when it is funded from the State Education Fund.

/E The four percent statutory reserve was eliminated for FY 2001-02. As much of the statutory reserve as necessary may be used to cover appropriations in FY 2002-03.

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- reduced the scheduled transfer to the Capital Construction Fund.

Based on the March 2003 forecast, these actions would have been sufficient to balance the FY 2003-04. However, because of the reduced revenue estimates, the budget will no longer be in balance. General Fund appropriations would need to be reduced by \$206.7 million in FY 2003-04.

“General Fund appropriations would need to be reduced by \$206.7 million in FY 2003-04.”

The federal government provided fiscal assistance to the states as part of the tax reduction package passed in May 2003. Colorado will receive \$146.3 million during federal fiscal years 2002-03 and 2003-04. Governor Owens announced a plan to utilize 90%, or \$131.7 million, of the federal assistance as a reserve fund in the event of future revenue downturns. This money could thus be used as an alternative to reducing appropriations by the full \$241.2 million in FY 2003-04. However, to the extent that the appropriations base is held

up, it would necessitate future reductions in appropriations in later years.

Meanwhile, additional future reductions were already anticipated based on the March forecast and legislative actions taken for FY 2002-03 and FY 2003-04. We now estimate that the budget shortfalls will be \$179.4 million and \$152.6 million, respectively. While options exist to balance the budget by reducing or postponing capital construction transfers and/or the payback to the CMTF, they would only delay the need to reduce General Fund appropriations. Meanwhile, appropriations would not reach the original appropriation of \$5.95 billion for FY 2002-03 until FY 2006-07.

If the budget balancing occurs through reduced appropriations, diversions of sales and use tax revenue could resume in FY 2006-07. A partial diversion would occur in that year and a full diversion would occur in FY 2007-08. A partial repayment of cash funds and small transfers to the Highway Users Tax Fund and Capital Construction Fund would occur in FY 2007-08.

Cash Fund Revenue Forecasts

- Total cash fund revenue subject to the TABOR revenue limit will increase 1.6% in FY 2002-03, and increase at an average annual rate of 5.5% over the forecast period.
- After increasing 4.2% in FY 2001-02, revenue to the **transportation-related** cash funds will decrease 3.0% in FY 2002-03 and increase at an average annual rate of 2.1% over the forecast period. Highway Users Tax Fund revenues will decrease slightly in FY 2002-03. Income subject to the TABOR spending limit in the State Highway Fund will decrease 39.6%, a result of smaller local government matching funds for transportation projects and substantially reduced interest earnings.
- Total **higher education** revenue will increase 11.5% in FY 2002-03, accompanied by 4.0% growth in full-time-equivalent student enrollment. Tuition revenue will increase 13.0% in FY 2002-03.
- Total **unemployment insurance** revenue will increase 17.0% in FY 2002-03. Tax revenues will increase 31.1% as a result of higher tax rates pushed up by recent large increases in benefit payments. After increasing 165.7% in FY 2001-02, benefits will increase 7.9% in FY 2002-03 and decrease at an average annual rate of 7.9% over the forecast period. The fund balance will fall to a level that will cause regular UI tax rates to increase over current levels for calendar years 2004 through 2006. In addition, the solvency tax will be levied in calendar years 2004 through 2007. The fund balance will increase at an average annual rate of 7.5% to \$968.6 million by FY 2007-08.
- **Limited Gaming Cash Fund** revenue will increase 0.9% in FY 2002-03. The recession in Colorado has lowered demand for gaming entertainment and snowstorms kept gamers away in February and March. The market has matured and gaming revenues will no longer increase at the double-digit pace seen in the late 1990s. Gaming revenues will increase at an average annual rate of 5.0% between FY 2001-02 and FY 2007-08.
- Finally, all **other cash fund** revenue will decrease 9.8% in FY 2002-03. These revenues will increase 17.8% in FY 2003-04, as fee bills enacted during the 2003 legislative session become effective. They will increase at an average annual rate of 4.5% over the forecast period.

Table 3
Cash Fund Revenue Estimates by Category, June 2003
Millions of Dollars

	Actual FY 01-02	Estimate FY 02-03	Estimate FY 03-04	Estimate FY 04-05	Estimate FY 05-06	Estimate FY 06-07	Estimate FY 07-08	FY 01-02 to FY 07-08 CAAGR *
Transportation-Related /A								
% Change	\$814.1 4.2%	\$790.1 -3.0%	\$821.4 4.0%	\$849.6 3.4%	\$878.4 3.4%	\$899.4 2.4%	\$924.9 2.8%	2.1%
Higher Education /B								
% Change	\$635.4 -9.7%	\$708.4 11.5%	\$766.0 8.1%	\$801.8 4.7%	\$845.2 5.4%	\$897.5 6.2%	\$952.9 6.2%	7.0%
Unemployment Insurance /C								
% Change	\$196.1 -2.4%	\$229.4 17.0%	\$349.0 52.2%	\$482.9 38.4%	\$526.3 9.0%	\$567.8 7.9%	\$425.3 -25.1%	13.8%
Limited Gaming Fund								
% Change	\$99.1 7.7%	\$100.0 0.9%	\$104.9 5.0%	\$111.9 6.7%	\$118.2 5.6%	\$125.6 6.2%	\$132.9 5.9%	5.0%
Capital Construction - Interest								
% Change	\$17.5 -49.8%	\$4.3 -75.6%	\$4.6 8.6%	\$8.8 90.7%	\$11.5 30.0%	\$8.0 -30.0%	\$5.7 -29.7%	-17.2%
Controlled Maintenance Trust Fund - Interest /E								
% Change	\$0.5 -97.1%	\$0.0	\$2.2	\$12.5 479.7%	\$24.6 96.8%	\$27.3 10.8%	\$29.3 7.4%	95.5%
Insurance-Related								
% Change	\$66.3 29.0%	\$61.4 -7.3%	\$56.2 -8.5%	\$60.3 7.4%	\$65.0 7.9%	\$70.2 7.9%	\$75.8 8.0%	2.3%
Regulatory Agencies								
% Change	\$50.4 -1.6%	\$50.7 0.6%	\$51.8 2.0%	\$53.2 2.7%	\$54.7 2.8%	\$56.3 2.9%	\$57.9 3.0%	2.3%
Severance Tax /D								
% Change	\$57.5 -23.1%	\$40.8 -29.0%	\$48.9 19.7%	\$45.0 -8.0%	\$46.4 3.2%	\$48.1 3.8%	\$49.7 3.2%	-2.4%
Employment Support Fund								
% Change	\$19.6 -6.0%	\$18.7 -4.5%	\$20.1 7.0%	\$20.7 3.2%	\$21.5 4.1%	\$22.5 4.6%	\$23.6 4.8%	3.1%
Petroleum Storage Tank Fund								
% Change	\$21.3 -19.9%	\$20.9 -1.8%	\$27.4 31.4%	\$22.2 -19.2%	\$22.8 2.8%	\$23.4 2.9%	\$12.1 -48.6%	-9.0%
Other Cash Funds								
% Change	\$254.6 -2.8%	\$243.1 -4.5%	\$307.0 26.3%	\$318.9 3.9%	\$338.2 6.0%	\$358.5 6.0%	\$381.2 6.3%	7.0%
Total Cash Fund Revenues Subject to the TABOR Limit	\$2,232.4 -6.1%	\$2,267.8 1.6%	\$2,559.5 12.9%	\$2,787.8 8.9%	\$2,952.8 5.9%	\$3,104.7 5.1%	\$3,071.3 -1.1%	5.5%

Totals may not sum due to rounding.

* CAAGR: Compound Average Annual Growth Rate.

/A This includes the Highway Users Tax Fund, the State Highway Fund, and other transportation-related funds.

/B Higher Education tuition revenues are net of scholarship allowances.

/C Includes a 20% tax credit on unemployment insurance taxes during calendar years 2001 and 2002. Reflects the solvency tax that will be triggered in calendar years 2004 through 2007.

/D This figure includes total severance tax revenue and interest earnings before distribution to the Local Government Severance Tax Fund.

/E The principal balance of the Controlled Maintenance Trust Fund, or \$243.9 million, was transferred to the General Fund on July 1, 2001. The CMTF will be repaid in two installments on July 1, 2004 and July 1, 2005. In addition, Senate Bill 03-342 required a \$40 million transfer from the General Fund to the Controlled Maintenance Trust Fund on July 1, 2003.

This section presents the forecasts for cash fund revenue subject to the TABOR revenue limit and describes several of the large cash funds. Table 3 presents a summary of all cash fund revenue subject to the TABOR revenue limit.

After decreasing 6.1% during FY 2001-02, total cash fund revenue subject to the TABOR revenue limit will increase 1.6% in FY 2002-03 and at an average annual rate of 5.5% over the forecast period. TABOR cash fund revenues will increase at strong rates in FY 2003-04 and FY 2004-05 as a result of numerous bills enacted during the 2003 session that increased fees and the unemployment insurance solvency tax, which will be levied in 2004 through 2007.

“TABOR cash fund revenues will increase at strong rates in FY 2003-04 and FY 2004-05 as a result of numerous bills enacted during the 2003 session....”

The forecast for cash fund revenues was reduced by \$30.4 million in FY 2002-03. Large decreases occurred in the forecasts for the umbrella group of other cash funds (\$27.1 million decrease), gaming taxes (\$5.1 million decrease), and severance taxes on oil and natural gas (\$9.0 million decrease).

Despite this decrease in the FY 2002-03 forecast, the forecast was increased by \$64.3 million in FY 2003-04, \$97.7 million in FY 2004-05, and by a total of \$496.9 million between FY 2003-04 and FY 2007-08. Fifty-three bills enacted during the 2003 legislative session will affect cash fund revenues subject to TABOR over the forecast period: 8 transferred money from various cash funds to the General Fund; 42 increased, enacted, or extended fees; two transferred money from the General Fund to the Controlled Maintenance Trust Fund; and one charged a fee to cash funds for investment services rendered by the Office of the State

Treasurer. These bills will decrease revenue subject to TABOR by a net \$4.6 million in FY 2002-03 and increase revenue by a net \$39.4 million and \$68.4 million in FY 2003-04 and FY 2004-05, respectively.

Other large increases occurred in the forecasts for higher education tuition and unemployment insurance taxes. Higher education in Colorado has seen record enrollment gains and a larger-than-usual increase in tuition rates. Thus, the forecast for higher education revenues increased by \$20.0 million in FY 2002-03, \$48.5 million in FY 2003-04, and by a total of \$362.7 million over the forecast period. The forecast for unemployment insurance taxes increased \$1.1 million in FY 2003-04, \$29.8 million in FY 2004-05, and by a total of \$122.1 million over the forecast period. The forecast for unemployment insurance taxes increased because the forecast for unemployment insurance benefit payments increased. Higher benefit payments increase tax rates in two ways: by reducing the UI fund balance to a level that shifts the tax rate schedule to a higher level and by increasing the tax rates for the individual employers that laid off those that claimed the benefits

Transportation-Related Cash Funds

Transportation-related cash funds, which include the Highway Users Tax Fund, the State Highway Fund, and several smaller funds, increased 4.2% in FY 2001-02. Transportation-related revenue will decrease 3.0% in FY 2002-03, and increase at an average annual rate of 2.1% between FY 2001-02 and FY 2007-08 (Table 4).

The Highway Users Tax Fund. The Highway User Tax Fund (HUTF) was created by the General Assembly as a result of the state constitutional requirement that the revenues from highway-related taxes and fees be used only for the construction, maintenance, and admini-

Table 4
Transportation Funds Revenue Forecast by Source, June 2003
 Millions of Dollars

	Actual FY 01-02	Estimate FY 02-03	Estimate FY 03-04	Estimate FY 04-05	Estimate FY 05-06	Estimate FY 06-07	Estimate FY 07-08	FY 2001-02 to FY 2007-08 CAAGR *
Highway Users Tax Fund								
Motor Fuel and Special Fuel Taxes % change	\$544.6 3.5%	\$543.7 -0.2%	\$557.1 2.5%	\$572.6 2.8%	\$588.8 2.8%	\$605.8 2.9%	\$622.7 2.8%	2.3%
Registrations % change	\$151.4 1.8%	\$156.3 3.3%	\$161.4 3.2%	\$168.5 4.4%	\$174.4 3.5%	\$179.6 3.0%	\$184.9 2.9%	3.4%
Other Receipts /A % change	\$43.7 0.6%	\$42.3 -3.2%	\$45.1 6.5%	\$47.9 6.2%	\$50.6 5.7%	\$53.3 5.3%	\$56.1 5.2%	4.2%
Accrual Adjustment /B	\$0.0	-\$6.8	-\$3.5	-\$1.7	\$0.0	\$0.0	\$0.0	NA
Total Highway Users Tax Fund % change	\$739.7 3.0%	\$735.6 -0.6%	\$760.1 3.3%	\$787.2 3.6%	\$813.9 3.4%	\$838.7 3.1%	\$863.6 3.0%	2.6%
State Highway Fund - Interest % change	\$50.1 17.0%	\$30.2 -39.6%	\$29.3 -3.0%	\$29.8 1.6%	\$30.9 3.8%	\$30.3 -1.9%	\$31.0 2.2%	-7.7%
Other Transportation Funds /C % change	\$24.3 21.5%	\$24.2 -0.4%	\$31.9 31.7%	\$32.6 2.2%	\$33.6 3.0%	\$30.3 -9.7%	\$30.4 0.1%	3.8%
TOTAL: All Transportation Funds % change	\$814.1 4.2%	\$790.1 -3.0%	\$821.4 4.0%	\$849.6 3.4%	\$878.4 3.4%	\$899.4 2.4%	\$924.9 2.8%	2.1%
Addendum:								
Senate Bill 97-1 Revenue /D % change	\$35.2 -82.2%	\$0.0 -100.0%	\$0.0 NA	\$0.0 NA	\$0.0 NA	\$0.0 NA	(\$0.0) NA	NA
Two-Thirds Excess General Fund Reserve /D	NA	\$0.0 NA	\$0.0 NA	\$0.0 NA	\$0.0 NA	\$0.0 NA	\$0.0 NA	NA

Totals may not sum due to rounding and do not include Senate Bill 97-1 revenues, which are 10.355 percent of sales and use tax revenues, or the transfer of two-thirds of the excess General Fund reserve. The Senate Bill 97-1 revenues and the transfer of two-thirds of the excess General Fund reserve are displayed in the General Fund and are then transferred to the HUTF.

* CAAGR: Compound Average Annual Growth Rate.

/A Includes interest receipts, judicial receipts, drivers' license fees, gross ton mile tax revenues, and other miscellaneous receipts in the HUTF. Incorporates the impacts of House Bill 01-1125, which institutes a new surcharge on first-time driver's license applicants, and Senate Bill 01-109, which reduces the motorist identification fee and extends it for two additional years.

B/ This is the estimated impact of a lawsuit that will reduce the accrual adjustment to the HUTF.

C/ Revenues received by these funds include fees for emissions, motorcycle safety, emergency medical services, and the state's motor vehicle titling and registration system. Incorporates the impact of HB 01-100, House Bill 02-1412, and HB 03-1432, which increase motor vehicle title fees to pay for computer upgrades. Two new funds are added to this group of cash funds in FY 2003-04 as a result of 2003 legislation. The Peace Officer Safety Training Board Cash Fund is added due to SB 03-103 and the new DOR License Plate Cash Fund is added due to SB 03-272.

D/ The Senate Bill 97-1 diversion will not occur after FY 2001-02. Neither will there be any money available in the excess General Fund reserve for transfer to the HUTF and Capital Construction.

stration of public highways. Thus, revenue sources for the HUTF include taxes on the sale of motor fuel (74%), automobile registration fees (20%), and revenues from the sale of driver's licenses, court fines, penalties, and interest income (6%).

After increasing 3.0% in FY 2001-02, total HUTF revenue will remain essentially flat in FY 2002-03 with a 0.6% decrease, and will increase at an average annual rate of 2.6% over the forecast period. The forecast for FY 2002-03 changed very little compared with the March forecast. The forecast was increased slightly in FY 2003-04 due to Senate Bill 03-192 and Senate Bill 03-239. Senate Bill 03-192 increased the fee required for restoration of suspended driving privileges and is expected to increase HUTF revenue by about \$0.8 million each year. Senate Bill 03-239 postponed the sunset of the fifty-cent motorist insurance identification fee from July 1, 2003, to July 1, 2008. The fee raises slightly more than \$2 million each year.

After increasing 3.5% in FY 2001-02, **motor fuel tax revenue** will be nearly flat in FY 2002-03, decreasing 0.2%. Lower net migration into the state, the employment recession, the manufacturing recession, and weak tourism will combine to slightly reduce motor fuel taxes in FY 2002-03. Healthier growth rates will resume as the economy recovers over remainder of the forecast period. Fuel tax revenue will increase at an average annual rate of 2.3% between FY 2001-02 and FY 2007-08.

“...fuel tax revenue will increase at an average annual rate of 2.3% between FY 2001-02 and FY 2007-08.”

Vehicle registration revenue, much of which is paid on larger and newer vehicles, will increase 3.3% in FY 2002-03 after increasing 1.8% during FY 2001-02. Much of this

growth, however, is due to a \$2.6 million accounting adjustment. The adjustment is a result of a substantial lag in information related to backfills from the General Fund for reduced registrations as a result of House Bill 00-1227. House Bill 00-1227 refunds part of the TABOR surplus by reducing registration fees and backfilling the HUTF for the lost revenue from the General Fund. Usually, this accounting adjustment would balance out over time. However, because there was no TABOR surplus in FY 2001-02, the refund mechanism is not occurring during FY 2002-03. Thus, the accounting adjustment will affect growth during FY 2002-03. Without the accounting adjustment, vehicle registration fees would have grown 1.6% during FY 2002-03.

Because of the zero-percent financing deals and other incentives offered by automobile dealerships, registration fees grew at extremely healthy rates that belied the recession in Colorado during the first few months of the fiscal year. However, by November, sales at most new and used auto dealerships had slowed considerably, and customers have not responded to incentives during the past six months as readily as they did in 2001 and much of 2002. Sales are expected to gradually improve from their current weak levels throughout the remainder of this year and grow at a somewhat healthier rate in 2004. Sales are expected to recover in 2005 and 2006 as consumers replace older cars. Registration fees will grow at an average annual rate of 3.4% over the forecast period.

The State Highway Fund. Once the taxes and fees generated by the HUTF are collected, they are disbursed to the state, counties, and cities in a manner stipulated by Colorado law. The state's share (approximately 55%) is credited to the State Highway Fund. Additionally, two-thirds of the excess General Fund reserve, the Senate Bill 97-1 diversion, and any capital construction transfers from the General Fund may be deposited into the State Highway Fund

each year. Interest earnings to the fund on these revenue sources are subject to the TABOR spending limit. Based on current law, General Fund revenues will not be sufficient for the Senate Bill 97-1 diversion and the transfer of two-thirds of the excess General Fund reserve to occur over the entire forecast period. In addition, the State Highway Fund has received a large amount of matching funds from local governments during the last few years for projects accelerated with the use of Transportation Revenue Anticipation Notes. These local matching funds will fall somewhat during FY 2002-03 from the peak amount received in FY 2001-02 and will decrease further during the next few years. Combined with substantially reduced interest earnings to the fund, this will cause State Highway Fund revenues subject to TABOR to decrease 39.6% in FY 2002-03 and decrease at an average annual rate of 7.7% over the forecast period.

Other Transportation Funds. These funds include the Air Account Fund, the Emergency Services Fund, the Motorcycle License Fund, and the Colorado State Titling and Registration (CSTARS) Fund. Two new cash funds have been added to this group as a result of legislation enacted during the 2003 legislative session. Senate Bill 03-103 added a 25-cent fee to most vehicle registrations statewide, beginning in FY 2003-04. The revenue will be deposited in the Peace Officer Safety Training (P.O.S.T.) Board Cash Fund, and is expected to generate about \$1.0 million dollars a year. Senate Bill 03-272 created a new cash fund and a new set of motor vehicle license plate fees to cover the costs of the Department of Revenue for issuing license plates. The License Plate Cash Fund is expected to generate \$6.5 million each year, beginning in FY 2003-04. Revenues to these funds will remain flat in FY 2002-03, and increase 31.7% in FY 2003-04 as the new revenue sources materialize. They will increase at an average annual rate of 3.8% over the forecast period.

Higher Education

In this section, we present the projections for cash fund revenue and full-time equivalent (FTE) student enrollment in the state's higher education system. This includes Colorado's public universities, colleges, and community colleges that receive state funds for operational costs. Tables 5 and 6 illustrate the estimates for higher education revenue and enrollment.

“Higher education cash fund revenue will increase a record 11.5% in FY 2002-03...”

Higher education revenue projections.

Higher education cash fund revenue will increase a record 11.5% in FY 2002-03, after increasing 8.6% in FY 2001-02. The expected growth in higher education revenue is due to record student enrollment as Coloradans seek to increase their jobs skills in light of poor employment prospects. Table 5 illustrates the tuition and nontuition revenue forecasts through FY 2007-08. Between FY 2001-02 and FY 2007-08, total higher education cash fund revenues will grow at an average annual rate of 7.0%.

Tuition revenue will increase 13.0% in FY 2002-03 after growing 10.1% in FY 2001-02. The last time the state saw two consecutive years of double-digit tuition growth was ten years ago, FY 1991-92 and FY 1992-93, when the state went through a recession. During times of economic slowdowns, the scarcity of jobs boosts college enrollment. We expect tuition revenue to jump another 9.5% in FY 2003-04 due to the broad discretion offered to higher education governing boards to set tuition rates for that year. From FY 2001-02 to FY 2007-08, tuition revenue will grow at an average rate of 7.3% per year.

Nontuition revenue, which includes student fees, auxiliary operations, and interest income,

Table 5
Higher Education Revenue Forecast by Source, June 2003
Millions of Dollars

	Actual FY 01-02	Estimate FY 02-03	Estimate FY 03-04	Estimate FY 04-05	Estimate FY 05-06	Estimate FY 06-07	Estimate FY 07-08	FY 2001-02 to FY 2007-08 CAAGR *
Tuition	\$602.6	\$680.8	\$745.2	\$773.5	\$814.5	\$864.7	\$921.2	7.3%
% change	10.1%	13.0%	9.5%	3.8%	5.3%	6.2%	6.5%	
Nontuition	\$161.6	\$168.0	\$174.5	\$187.9	\$198.6	\$211.2	\$221.7	5.4%
% change	3.3%	4.0%	3.9%	7.6%	5.7%	6.3%	5.0%	
Scholarship Allowance Deductions	(\$128.8)	(\$140.4)	(\$153.7)	(\$159.6)	(\$168.0)	(\$178.4)	(\$190.0)	6.7%
% change	NA	9.0%	9.5%	3.8%	5.3%	6.2%	6.5%	
TOTAL Higher Education Cash	\$635.4	\$708.4	\$766.0	\$801.8	\$845.2	\$897.5	\$952.9	7.0%
Percent change	8.6%	11.5%	8.1%	4.7%	5.4%	6.2%	6.2%	

* CAAGR: Compound Average Annual Growth Rate.

Notes: Totals may not sum due to rounding.

Beginning in FY 2002-03, scholarship allowances were no longer counted as revenue under TABOR. This was accompanied by a one-time adjustment to exclude scholarship allowances from the FY 2001-02 TABOR base.

Table 6
Higher Education Enrollment Forecast, June 2003
Public Higher Education Full-Time-Equivalent (FTE) Student Enrollment

	Actual FY 01-02	Estimate FY 02-03	Estimate FY 03-04	Estimate FY 04-05	Estimate FY 05-06	Estimate FY 06-07	Estimate FY 07-08	FY 2001-02 to FY 2007- 08 CAAGR *
Residents	122,062	129,189	131,722	133,276	134,431	136,368	138,101	2.1%
% change	4.1%	5.8%	2.0%	1.2%	0.9%	1.4%	1.3%	
Nonresidents	21,911	21,928	21,769	21,629	21,856	22,191	22,589	0.5%
% change	3.2%	0.1%	-0.7%	-0.6%	1.0%	1.5%	1.8%	
TOTAL FTE Student Enrollment	143,972	151,117	153,491	154,905	156,286	158,558	160,690	1.8%
Percent change	4.0%	5.0%	1.6%	0.9%	0.9%	1.5%	1.3%	

* CAAGR: Compound Average Annual Growth Rate.

Totals may not sum due to rounding.

will maintain a healthy growth pattern throughout the forecast period, increasing 4.0% in FY 2002-03 and 3.9% in FY 2003-04. Through FY 2007-08, nontuition revenue will grow at an average annual rate of 5.4%.

Higher education enrollment projections.

Enrollment is projected to increase 5.0% in FY 2002-03, after a 4.0% gain in FY 2001-02. The FY 2002-03 enrollment gain will be the largest in 20 years. Enrollment surged this year as workers abandoned the weak job market and chose to improve their employment skills. As the economy improves, enrollment gains will taper. Total student enrollment at Colorado's public higher education institutions will increase at an average annual rate of 1.8% between FY 2001-02 and FY 2007-08. Table 6 displays the FTE student enrollment projections by residency status.

“Resident enrollment will increase at a 20-year record pace of 5.8% in FY 2002-03...”

Resident enrollment will increase at a 20-year record pace of 5.8% in FY 2002-03 as the economic slowdown continued to drive people from the labor force to education in order to obtain more marketable skills. As a result of recovering employment in 2004, enrollment growth will taper through the remainder of the forecast period. Resident enrollment will increase at an average annual rate of 2.1% between FY 2001-02 and FY 2007-08.

Nonresident enrollment in FY 2002-03 will be nearly unchanged from last year's enrollment, rising a scant 0.1%. Growth will be slower than resident enrollment because the rising cost of out-of-state tuition will influence potential nonresident enrollees to attend a school in their home state or become Colorado residents. This would have occurred last year if not for the recession, which caused nonresidents and residents to seek additional educa-

tional opportunities. The slower growth is also attributable to lower levels of migration in 2003 and 2004. Once migration recovers in 2005, nonresident enrollment growth will revive in FY 2005-06 and beyond. Nonresident enrollment will increase modestly at an average annual rate of 0.5% between FY 2001-02 and FY 2007-08.

Changes from prior forecasts. The revenue forecast for FY 2002-03 is higher than the March 2003 estimate due to a larger-than-expected tuition and nontuition cash flow through April 2003. The revenue forecast for FY 2003-04 is also higher than the previous forecast due to the broader tuition caps given to higher education governing boards.

Factors affecting the forecast. Demographic factors, such as the number of high school graduates, are significant indicators of potential higher education enrollment. Other demographic factors include: the number of Coloradans in college-age groups; the level of migration into the state; the number of Coloradans in particular age groups; and population growth in regions close in proximity to colleges and universities.

Economic variables also drive the forecast of higher education enrollment. During the economic slowdown, enrollment increased as employees sought to improve their marketable skills. This occurred in both undergraduate and graduate programs. Graduate programs saw enrollment gains as professionals returned to seek advanced degrees. The economic slowdown also affected undergraduate attendance at both four-year and two-year schools, as high school graduates had a more difficult time finding employment without a college degree.

The cost of tuition is also a factor affecting enrollment, particularly between institutions. However, out-of-state enrollment has histori-

cally been only marginally influenced by tuition increases because nonresidents have chosen Colorado schools for reasons other than tuition costs. In the last five years, the University of Colorado at Boulder has maintained the fourth highest nonresident undergraduate tuition among public research universities, behind Michigan, Vermont, and Virginia. Among western states only, FY 2002-03 CU-Boulder nonresident tuition was 14% higher than California nonresident tuition, the next highest tuition in the region. Despite the cost of nonresident tuition, the University of Colorado at Boulder estimates an 11% increase in applications for nonresident undergraduate enrollment.

“University of Colorado at Boulder has maintained the fourth highest nonresident undergraduate tuition among public research universities...”

Tuition revenue is driven by enrollment, inflation, and legislative and/or executive branch decisions regarding tuition growth caps. Non-tuition revenue is driven by student fees, on-campus consumption, housing, and auxiliary operations such as university clinics. Interest income also contributes significantly to non-tuition revenue.

Changes in financial reporting: scholarship allowances. In 1999, the Governmental Accounting Standards Board (GASB) issued statements 34 and 35, requiring institutions of public higher education to report scholarship allowances and tuition discounts as transfers rather than revenue. This accounting change became effective at the end of FY 2001-02 and applied to financial aid for student tuition, fees, and housing provided through state or federal sources. This change was accompanied by an adjustment to the FY 2001-02 TABOR base to calculate an accurate revenue growth rate. Scholarship allowances totaled \$128.8 million, or 20.3% of all higher education cash funds. As a result, \$128.8 million

was deducted from FY 2001-02 higher education cash funds for the purposes of calculating a consistent TABOR base. Scholarship allowance deductions are estimated to be \$140.4 million in FY 2002-03 and \$153.7 million in FY 2003-04.

Changes in financial reporting: summer school tuition. GASB statements 34 and 35 also required public higher education institutes to report summer session tuition monthly rather than at the end of the summer term. As a result, revenue collected in early summer terms (May and June) that would have been reported in FY 2002-03 was reported in FY 2001-02. This inflated FY 2001-02 revenue because it included *all* of the 2001 summer tuition and *part* of the 2002 summer tuition.

Legislation affecting the forecast. The June forecast reflects the tuition inflation caps approved for FY 2003-04. The General Assembly authorized a 10% increase in resident and nonresident tuition, compared with the 2002 Denver-Boulder-Greeley inflation rate of 2.0%. This was done to help balance the FY 2003-04 budget shortfall in which there were insufficient General Fund revenues. A larger tuition growth cap allowed higher education institutions to fund expenses by raising tuition revenue to replace the reduced General Fund appropriation.

The FY 2003-04 tuition caps were vetoed by the Governor, who directed the Colorado Commission on Higher Education (CCHE) to determine the ceilings for tuition increases. As a result, the resident tuition rate increases were capped at 5% for most four-year and two-year colleges (with the exceptions of Fort Lewis College, capped at 7%, and the Colorado School of Mines, capped at 8.7%) and 10% for research institutions such as the University of Colorado system, the Colorado State University system, and the University of Northern Colorado. Nonresident tuition was capped at 10%. The CU-Boulder campus was

also allowed an additional 5% tuition increase for a program to fund student financial aid, improve academic programs, and bolster faculty salaries. Future per-pupil tuition is assumed to increase at the projected Denver-Boulder-Greeley inflation rate.

Unemployment Insurance Trust Fund

Forecasts for unemployment insurance tax revenue, benefit payments, and the Unemployment Insurance (UI) Trust Fund balance are shown in Table 7. The UI Fund collects taxes from employers and uses the revenue for unemployment benefits. Growth in UI taxes depends upon employment and wage growth, the rate at which covered employees switch employers, the level of the UI Trust Fund balance, and the amount of benefits paid to UI claimants in the past. The amount of benefits paid to UI claimants depends upon the number of unemployed and the average wage level from the prior calendar year. When the amount of benefits paid in the past rises, the effective UI tax rate paid by all employers rises, all else equal.

The amount in which taxes increase when wages increase is muted, since the tax base is capped at the first \$10,000 in wages paid to each covered employee per employer during the calendar year. However, wage growth in any calendar year has a significant effect on benefit payments two years later, and thus on the UI tax rate four years after the original calendar year in which wages increased. For example, total private wages in Colorado increased 13.0% and 12.5% during calendar years 1999 and 2000, respectively. Taxable wages increased 7.3% and 5.8% during 1999 and 2000, and were boosted by an extremely mobile work force that changed jobs readily. However, along with mass layoffs, this wage growth contributed to a 165.7% increase in benefit payments during FY 2001-02. This

contributed to an estimated relative increase of 37.7% in the effective UI tax rate for calendar year 2003. Benefit payments are expected to increase 7.9% in FY 2002-03, and the effective tax rate will increase in 2004 as well.

UI background. The current situation for UI taxes, benefits, and the UI fund balance was caused by the dramatic turnaround in Colorado's economy in 2001. Going into 2000, UI tax rates were at historic lows as a result of extremely low benefit payments during the late 1990s. Layoffs began to accelerate during the first half of 2001. The layoffs, combined with the strong wage growth that occurred in 1998 and 1999, caused benefit payments to increase 18.0% in FY 2000-01. Continuing layoffs in late 2001 and the first half of 2002, combined with the strong wage growth in 1999 and 2000, culminated in a 165.7% increase in benefit payments during FY 2001-02.

“...continuing layoffs in late 2001 and the first half of 2002 culminated in a 165.7% increase in benefit payments during FY 2001-02.”

Meanwhile, tax revenues had not yet reacted to the high level of benefit payments caused by the increased layoffs. Combined with decreases in taxable wages and a temporary 20% tax credit, UI taxes decreased 15.9% in FY 2000-01 and were essentially flat in FY 2001-02. Interest earnings to the fund were strong during FY 2000-01, but have been falling ever since. Thus, the fund balance began dropping from its high of \$801.9 million in September 2001 to \$626.9 million by June 2002. The fund balance was only 0.91% of total private wages in 2001. It would have fallen substantially further if not for a \$142.7 million Special Reed Act transfer from the U.S. Department of Labor. A solvency tax is triggered in Colorado when the UI fund balance as a percentage of total annual private wages in the preceding calendar year is at or below 0.9%. Thus, the UI

Table 7
Unemployment Insurance Trust Fund Forecast, June 2003
Revenues, Benefits Paid, The UI Fund Balance, and Solvency

Millions of Dollars

	Actual FY 01-02	Estimate FY 02-03	Estimate FY 03-04	Estimate FY 04-05	Estimate FY 05-06	Estimate FY 06-07	Estimate FY 07-08	FY 2001-02 to FY 2007-08 CAAGR *
Beginning Balance	\$794.1	\$626.9	\$323.8	\$238.7	\$374.0	\$576.1	\$837.3	0.9%
Plus Income Received								
Taxes /A	\$150.7	\$197.5	\$282.1	\$359.2	\$323.0	\$272.7	\$268.9	10.1%
Solvency Taxes /B	\$0.0	\$0.0	\$40.9	\$102.9	\$170.9	\$245.4	\$84.2	
Interest	\$45.4	\$31.9	\$26.1	\$20.8	\$32.4	\$49.7	\$72.2	8.0%
Total Revenues	\$196.1	\$229.4	\$349.0	\$482.9	\$526.3	\$567.8	\$425.3	13.8%
% change	-2.6%	17.0%	52.2%	38.4%	9.0%	7.9%	-25.1%	
Less Benefits Paid	(\$486.8)	(\$525.5)	(\$439.6)	(\$351.9)	(\$328.2)	(\$310.4)	(\$297.6)	-7.9%
% change	165.7%	7.9%	-16.4%	-19.9%	-6.7%	-5.4%	-4.1%	
Federal Reed Act Transfer /C	\$142.7	(\$13.4)	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	NA
Accounting Adjustment/D	(\$19.1)	\$6.5	\$5.4	\$4.3	\$4.0	\$3.8	\$3.7	NA
Ending Balance	\$626.9	\$323.8	\$238.7	\$374.0	\$576.1	\$837.3	\$968.6	7.5%
Solvency Ratio:								
Fund Balance as a Percent of Total Annual Private Wages /B	0.91%	0.49%	0.35%	0.51%	0.74%	1.01%	1.09%	3.1%

Totals may not sum due to rounding.

NA: Not Applicable.

* CAAGR: Compound Average Annual Growth Rate.

/A This includes taxes from private employers and state and local governments, penalty receipts, and the accrual adjustment on taxes. 50% of the surcharge is also included except for during FY 2003-04 and the last quarter of FY 2002-03, per Senate Bill 03-239. It incorporates a 20% tax credit for eligible employers in calendar years 2001 and 2002. The tax credit will not be in effect after 2002.

/B The solvency tax is triggered when the fund balance as a percent of total annual private wages falls below 0.9%. Solvency tax estimates made by the Colorado Department of Labor and Employment.

/C One-time special Reed Act distribution from the Federal Unemployment Insurance Trust Fund. This transfer is assumed to be spent on benefits until otherwise appropriated by the General Assembly. SB 03-207 appropriated \$13.4 million for employment training purposes.

/D This is the accrual adjustment for benefits paid and other accounting adjustments.

fund balance was just barely large enough to prevent the solvency tax from starting in 2003.

UI tax forecast. Tax revenues will show a varied pattern of growth over the forecast period. While the original 20% tax credit expired at the end of 2002, it was extended on a conditional basis. The tax credit is in effect if the fund balance at fiscal-year-end is at least 1.1% of total private wages during the preceding calendar year. The 20% tax credit on regular UI taxes will not occur starting in calendar year 2003 and throughout the entire forecast period.

“The solvency tax will be levied during calendar years 2004 through 2007.”

Meanwhile, the solvency tax will be levied during calendar years 2004 through 2007. The fund balance will fall to an estimated 0.49% of 2002 total wages at the end of FY 2002-03 and will not return to solvency until the end of FY 2006-07. During calendar year 2003, the UI tax rate is reacting to the huge increase in benefits in recent years, and combined with the absence of the 20% tax credit, will increase 37.7%. Combined with a decrease in taxable wages, this will cause UI tax revenues to increase 31.8% in FY 2002-03.

The effective tax rate will increase for two reasons in calendar year 2004. First, individual employers rates will increase again as a result of increases in benefit payments made during FY 2002-03. In addition, the fund balance will drop to a level that triggers a higher tax schedule. Tax rates for most employers increase each time the fund balance falls below 12 different thresholds, the highest of which is \$450 million. A projected fund balance of \$323.8 million will cause the tax rate schedule to shift from the lowest in 2003 to the sixth highest in 2004. The effective tax rate is expected to increase 33.1% as a result of the schedule change. Taxes will increase 63.5% in FY

2003-04 and 43.1% in FY 2004-05 as tax rates continue to rise due to high levels of benefit payments and a low fund balance, and the solvency tax is levied beginning in January 2004.

While revenues from the regular UI tax will begin to decrease in FY 2005-06, total UI taxes will increase in FY 2005-06 and FY 2006-07 because solvency tax revenues will continue to increase at strong rates. Tax revenues will finally fall off 31.9% in FY 2007-08 with the removal of the solvency tax on January 1, 2008. In addition, the tax rate schedule will shift back to the lowest rate schedule in calendar year 2007. Over the forecast period, tax revenues will increase at an average annual rate of 15.3%.

UI benefits forecast. After increasing 165.7% in FY 2001-02, benefits will increase 7.9% in FY 2002-03 and begin decreasing thereafter as the employment-recession recedes. Over the forecast period, benefits will decrease at an average annual rate of 7.9%.

The UI Trust Fund balance. The UI Fund balance will fall to \$323.8 million on June 30, 2003, as a result of extremely high benefit payments and tax revenues that have just begun to react to the high level of benefit payments seen in the past few years. The solvency tax will begin to be levied in 2004. The solvency tax will be levied for four years through 2007. Because of the solvency taxes and the increased tax rates, the fund balance will begin to grow again. The fund balance will increase at an average annual rate of 7.5% over the forecast period to \$968.6 million at the end of FY 2007-08.

“A projected fund balance of \$323.8 million will cause the tax rate schedule to shift from the lowest in 2003 to the sixth highest in 2004...”

Senate Bill 03-296 will reduce the level of the fund balance by an estimated \$6.7 million in

FY 2002-03 and \$20.1 million in FY 2003-04. The bill diverted 50% of the unemployment insurance surcharge tax from the UI Trust Fund to the General Fund between May 1, 2003, and June 30, 2004.

The Special Reed Act Transfer. In 2002, Congress enacted H.R. 3090, which, among other things, distributed a total of \$8 billion from the federal UI trust fund to the state UI trust funds. Colorado received \$142.7 million of this distribution, known as the Special Reed Act Transfer. The Department of Labor and Employment placed this money into Colorado's trust fund in late FY 2001-02 until further notice. Senate Bill 03-207 appropriated \$13.4 million of this revenue for employment training purposes. This forecast assumes that the remainder of the transfer remains in the fund for the duration of the forecast period.

Overview of Additional Cash Funds

This section provides brief descriptions of other large cash funds that are subject to the TABOR spending limitation. In FY 2001-02, these cash funds comprised 26.3% of total cash fund revenue. The forecast for each of these funds is contained in Table 3.

The ***Limited Gaming Fund*** receives license fees from gaming-related employees, vendors, and casinos and taxes levied on the adjusted gross proceeds (AGP) earned from gaming activity in Black Hawk, Central City, and Cripple Creek.

Gaming revenue will increase a mere 0.9% in FY 2002-03. Larger casinos, which pay a higher tax rate than smaller casinos, continue to gain market share in the gambling towns. However, the recession in Colorado is reducing demand for gaming entertainment this year and several snowstorms kept gamblers away in February and March. In addition, interest earnings and fee revenues to the fund are substantially lower this year than in FY 2001-02.

The gaming market in Colorado has matured somewhat, and growth will be subdued over the remainder of the forecast period relative to the double-digit rates seen in the late 1990s. Gaming revenue will increase at an average annual rate of 5.0% between FY 2001-02 and FY 2007-08.

“The gaming market in Colorado has matured somewhat, and growth will be subdued over the remainder of the forecast period...”

The ***Capital Construction Fund*** retains money for the construction of projects such as prisons and higher education facilities. Income to this fund is comprised largely of interest earnings on the unspent balance. A substantial portion of the fund was transferred to the General Fund in FY 2001-02 due to state budget problems. Additionally, Senate Bill 03-179 transferred another \$29.6 million from the Capital Construction Fund to the General Fund in March. Of this amount, \$25.3 million came from the fund balance and \$4.3 million was interest earned in the fund in FY 2002-03 prior to the date of transfer. The bill also directed that all interest earnings to the fund after the bill's enactment date be diverted away from the Capital Construction Fund to the General Fund through the end of the fiscal year.

A total of \$9.4 million will be transferred from the General Fund to the Capital Construction Fund in FY 2003-04. Approximately \$100 million in annual transfers scheduled in FY 2004-05 and FY 2005-06 remains intact in current law. Interest earnings to the fund will fall from \$17.5 million in FY 2001-02 to \$4.3 million in FY 2002-03 and \$4.6 million in FY 2003-04. The fund balance will grow slowly throughout the forecast period, but will continue to remain substantially lower than levels seen prior to FY 2001-02. Therefore, we expect income to the Capital Construction Fund to decrease at an average annual rate of 17.2% between FY 2001-02 and FY 2007-08.

The Department of *Regulatory Agencies* regulates and enforces Colorado laws regarding various industries in Colorado. The department collects license and other fees from the professions that it regulates. Fee revenue is expected to increase 0.7% in FY 2002-03. Interest earnings to this group of cash funds will be reduced modestly due to a \$1.3 million transfer from the PUC Motor Carrier Cash Fund in March 2003 to the General Fund per Senate Bill 03-191. Five additional bills enacted during the 2003 legislative session will increase fee revenue to this group of cash funds by an estimated total of \$450,000 in FY 2003-04. Because most fees are related to employment levels, DORA cash fund revenue will increase modestly during the remainder of the forecast period.

“Premiums on workers compensation insurance policies have grown during the past few years, and thus taxes on the premiums increased 29.0% in FY 2001-02...”

Insurance-related taxes are deposited into three cash funds administered by the Division of Workers Compensation in the Department of Labor and Employment. These taxes are imposed on workers compensation insurance premiums. Premiums on workers compensation insurance policies have grown during the past few years, and thus taxes on the premiums increased 29.0% in FY 2001-02. However, premium rates decreased in FY 2002-03, and interest earnings have decreased substantially as well due to the transfer of \$75 million from the Major Medical Fund to the General Fund in July. Thus, these revenues will decrease 7.3% in FY 2002-03. Interest earnings will continue to fall by a net \$7.2 million due to transfers from the Major Medical Fund and Subsequent Injury Fund to the General Fund per Senate Bill 03-191. Senate Bill 03-191 directed that \$150 million and \$20 million be transferred to the General Fund from the Major Medical Fund and the Subsequent Injury Fund, respectively, in May 2003. Ten million

dollars will be transferred back to the Major Medical Fund on July 1, 2003. Healthier growth rates will resume after FY 2003-04, and these revenues will increase at an average annual rate of 2.3% over the forecast period.

Severance taxes are levied on the value of extracted oil, natural gas, coal, and minerals. Final oil and gas severance taxes for a given year are reduced by a portion of a company's property taxes paid during the same year, but based on the previous year's income. Because the value of oil and gas can change substantially over the course of two years, this credit can alternately be very large or small relative to a taxpayer's severance tax liability, and thus a volatile collections pattern can occur.

Total severance tax revenues, including interest earnings, have seen two years of abnormally high collections due to a concurrent spike in oil and gas prices and production, much of which occurred due to a federal subsidy that will no longer be available to most production in Colorado in the future. Prices for natural gas and oil fell substantially in 2002 over their high levels in 2001. Combined with the relatively high costs faced by Colorado producers due to limited pipeline capacity, this caused some producers to scale back on production during 2002. In addition, property taxes paid in FY 2002-03 have been substantially higher than those paid in FY 2001-02, since natural gas production and prices were high in 2000 and 2001. Thus, despite higher natural gas prices during the first half of 2003, oil and gas severance tax revenues will decrease 38.4% in FY 2002-03.

Meanwhile, natural gas prices are expected to remain high well into 2004. Production has ramped up, and property taxes paid in FY 2003-04 on production in 2002 will be relatively low. Thus, severance taxes on oil and gas will increase 34.5% in FY 2003-04. Total severance taxes, excluding interest earnings, will decrease 31.1% in FY 2002-03, increase

26.0% in FY 2003-04, and decrease at an average annual rate of 2.5% over the forecast period.

“natural gas prices are expected to remain high well into 2004...”

Interest earnings have fallen substantially due to a \$20.2 million transfer in FY 2001-02 from the Severance Tax Trust Fund to the General Fund. Interest earnings will remain low in FY 2003-04 and FY 2004-05 as a result of two bills. Senate Bill 03-191 directed that \$7.1 million be transferred from the Severance Tax Trust Fund to the General Fund on June 30, 2003. Senate Bill 03-271 directed that an additional \$4.6 million be transferred on June 30, 2004. After decreasing 23.1% in FY 2001-02, all severance taxes and interest income will total \$40.8 million in FY 2002-03, a 29.0% decline. Between FY 2001-02 and FY 2007-08, total severance tax revenues will decrease at an average annual rate of 2.4%.

The ***Employment Support Fund*** (ESF) is designed to help maintain the solvency of the Unemployment Insurance Trust Fund. The ESF receives its revenue from the unemployment insurance surcharge tax. The surcharge tax is levied to cover benefits charged against employers who have gone out of business. After declining 6.0% in FY 2001-02, ESF revenues will decrease 4.5% in FY 2002-03 and increase at an average annual rate of 3.1% over the forecast period.

The ***Petroleum Storage Tank Fund*** collects money to clean leaking underground gasoline storage tanks. Most of the fees collected in the fund are levied on tank truckloads of fuel products shipped within the state. The fee level is set in statute to fluctuate with the amount of money in the fund's reserve. The fee was \$75 during FY 2000-01 because of demand on the fund's resources. Demands for the money in the fund eased up in early FY

2001-02, and the fee dropped to \$50 on October 1, 2001. Demand on the fund's resources have accelerated in early 2003 and the fee increased to \$75 again on March 1, 2003. Demands on the fund's resources are expected to remain at high levels for at least a year. After decreasing 19.9% in FY 2001-02, revenues will decrease an additional 1.6% in FY 2002-03. Assuming that the fee will be at \$75 for the entire fiscal year, revenues to the fund will increase 31.4% in FY 2003-04. House Bill 03-1099 will increase fee revenue to the fund by an estimated \$219,399 in FY 2003-04. The bill revised the fee by requiring that every first purchaser of liquified petroleum gas pay a fee of \$10 per tank truckload. In addition, the forecast for this fund was increased by a total of \$37.9 million over the forecast period as a result of Senate Bill 03-324. This bill postponed when the fee is reduced to \$25, subject to the requirement that the fund balance is less than \$8 million, from July 1, 2004, to July 1, 2007. Revenues to the Petroleum Storage Tank Fund will decrease at an average annual rate of 9.0% between FY 2001-02 and FY 2007-08.

The ***Controlled Maintenance Trust Fund*** (CMTF) is a state trust fund from which the interest earned may be spent for maintenance of existing state facilities. Interest earnings to the CMTF have shown a volatile pattern as a result of House Bill 01-1267, House Bill 02-1446, and House Bill 02-1391. House Bill 01-1267 transferred the principal balance of the CMTF (\$243.9 million) to the General Fund on July 1, 2001. While House Bill 01-1267 originally scheduled the payback of \$267.4 million to the fund on July 1, 2002, state budgetary problems prevented that. Thus, House Bill 02-1446 postponed the payback. Meanwhile, House Bill 02-1391 transferred \$9.5 million to the General Fund in March 2002, leaving less than \$300,000 in the CMTF. Senate Bill 03-262 directed that the \$276.4 million be repaid in two installments on July 1, 2004,

and July 1, 2005. Thus, interest income to the CMTF fell to \$0.5 million in FY 2001-02 and will be minimal in FY 2002-03. The CMTF will generate \$2.2 million in FY 2003-04 due to Senate Bill 03-342, which required that \$40 million be transferred from the General Fund to the CMTF on July 1, 2003. Over the forecast period, interest income to the fund will recover as the principal is paid back.

Note that this forecast assumes that the sale and subsequent lease-purchase of government buildings pursuant to Senate Bill 03-342 does not occur. Senate Bill 03-342 authorizes the Department of Personnel and Administration, with the approval of the Office of State Planning and Budgeting and the State Treasurer, to sell one or more state facilities to raise up to \$160 million of net proceeds for the state for a cash flow reserve. The \$160 million would be deposited into the CMTF. The General Assembly also enacted Senate Bill 03-268, which authorizes the State Treasurer, State Controller, and Director of the Office of State Planning and Budgeting to agree to securitize a portion of the state's stream of tobacco settle-

ment payments to raise \$160 million of net proceeds for a cash flow reserve. Our perceived intent of the General Assembly is that only one of the two scenarios authorized above would occur.

The "*other cash funds*" component includes nearly 200 smaller cash funds and can be quite volatile. These funds decreased 2.8% as a group in FY 2001-02, and will decrease 4.5% in FY 2002-03. The decrease in FY 2002-03 is due to the reclassification of \$25 million from TABOR revenue to TABOR exempt revenue: \$15 million in the Unclaimed Property Trust Fund and, per House Bill 02-1171, \$10.3 million in the Library and Canteen Trust Fund. Revenues to this group of cash funds will be increased by a net amount of \$4.7 million in FY 2002-03 as a result of six bills enacted during the 2003 legislative session. Revenues to these funds will increase 26.3% in FY 2003-04 as a total of 35 bills increases revenue by a net amount of \$53.4 million. Over the forecast period, revenues to these funds will increase at an average annual rate of 7.0%.

The Constitutional Revenue Limit

- After exceeding the constitutional revenue limit for five consecutive years through FY 2000-2001, the state will now fall short of its limit for the second consecutive year during FY 2002-03. The state will also fail to have a surplus in FY 2003-04 due to the population adjustment that will have its first impact that year.
- Due to the reduction of the allowable limit during FYs 2001-02 and 2002-03 (often called the "ratchet down"), the state will again see surpluses beginning in FY 2004-05 and throughout the remainder of the forecast period. The state will refund an estimated \$1.3 billion to taxpayers over that time period.
- The state will utilize just two of its 19 refund mechanisms to refund the FY 2004-05 surplus in the following fiscal year. As the TABOR surplus increases, more mechanisms will be used. The state will use five mechanisms during FY 2006-07 and 11 mechanisms in FY 2007-08.

The provisions of Article X, Section 20 of the Colorado Constitution (TABOR) require that revenue collected above the TABOR limit be refunded to taxpayers within one year after the FY in which they were collected. TABOR limits annual growth in most state revenue to inflation plus the annual percentage change in population.

The state first had a TABOR surplus in FY 1996-97 and refunded \$3.3 billion to taxpayers during that year and the following four years as the economy boomed and the state experienced very strong revenue growth. During the current economic recession, however, the state has been unable to collect revenue equal to its revenue limit as the state's taxpayers taxable incomes, spending, and capital gains earnings declined and tax cuts were implemented. As a result, the state fell \$365.7 million short of its allowable limit during FY 2001-02. We project that the state's revenue will fall \$703.6 million below its TABOR limit during FY 2002-03.

“... the state's revenue will fall \$703.6 million below its TABOR limit during FY 2002-03.”

The “ratchet down” effect. Allowable revenue each year is based on the lesser of actual revenue in the prior year or the prior year's limit increased by the sum of the Denver-Boulder-Greeley inflation rate and the state-wide population growth rate. Therefore, whenever revenue collections fall below the limit in one year, the limit for the next year is calculated from a lower base than would have been the case if revenue had met or exceeded the limit. This phenomenon is known as the “ratchet down” effect of TABOR. In fact, due to the ratchet down of the limit during FYs 2001-02 and 2002-03, the state's TABOR limit in FY 2004-05 will be roughly equal to the limit for FY 1999-00. Meanwhile, the state's population will have increased by 8.9% during that period and inflation will be up 15.2%.

The population adjustment. During the 1990s, the federal government underestimated Colorado's population. Therefore, the state allowed for too little population growth when calculating its TABOR limit during the years that the state had surplus revenue. As a result, the state refunded \$483 million more to taxpayers during the late 1990s than would have been necessary had the correct population growth been calculated. TABOR allows for the limit to be adjusted each decade in accordance with the Census count.

The General Assembly determined that the adjustment process would be to carry forward six percentage points of population growth that were unused after the 2000 Census and use those points when revenue allows. We project that 3.1 percentage points will be used during FY 2003-04, allowing the state to retain an additional \$236.9 million of revenue. The remaining 2.9 percentage points will be used in FY 2004-05 to retain an incremental increase of \$232.6 million. The combined impact of both years' adjustments will allow the state to keep an additional \$477.2 million in FY 2004-05. Since the adjusted amount is built into the state's TABOR base, the state will continue to keep more revenue than otherwise would have been the case each year into the future as long as the state does not experience another ratchet down.

“... the state will continue to keep more revenue than otherwise would have been the case each year into the future as long as the state does not experience another ratchet down.”

Estimates of the TABOR surplus. Despite the population adjustment in FY 2004-05, the state will still receive more revenue than it can keep that year. As a result, the state will have a \$113.6 million surplus that will be refunded during FY 2005-06. Only the earned income tax credit and the sales tax refund mechanisms will be used to refund the money that year.

The state's surplus will grow to \$341.5 million in FY 2005-06 and \$477.4 million in FY 2006-07. The state will use five and eleven refund mechanisms during those years. Table 8 shows the estimated TABOR surplus amounts for each year of the forecast, while Table 9 shows a detailed calculation of the limits and surpluses. In the absence of the population adjustment, the state would have collected surpluses of \$236.9 million in FY 2003-04, \$590.8 million in FY 2004-05, and \$839.2 million in FY 2005-06. Those refund levels would have resulted in the use of five refund mechanisms the first year and all nineteen of the mechanisms in the other years.

Table 8
Estimated TABOR Surplus Revenues
(millions of dollars)

Fiscal Year	Amount
FY 2002-03	\$0.0
FY 2003-04	\$0.0
FY 2004-05	\$113.6
FY 2005-06	\$341.5
FY 2006-07	\$477.4
FY 2007-08	\$394.7

Reversal of House Bill 98-1414. During the 2003 legislative session, the General Assembly reversed the accounting of the TABOR refund from what was done under House Bill 98-1414. That bill allowed the state to account for the TABOR refund only in the year it was refunded, not the year it was collected. This allowed the state to spend the TABOR surplus in the year it was collected as long as the refund was made from revenue collected the following year. This system worked well and allowed for extra spending during the years in which the TABOR surplus continued to get bigger each year. However, when the surplus disappeared in FY 2001-02 but a large refund was still owed from the prior year, the state's budget felt the dual impact of a drop in revenue and a large liability for the surplus that had actually been collected during the prior year.

“Enactment of House Bill 03-1238 means that the required cuts to the General Fund in FY 2004-05 will be \$179.4 million rather than \$70.3 million as would have otherwise been the case.”

Reversing this system and going to an accrual method of accounting for the surplus, which means that the revenue is accounted for during the year it is collected rather than the year it is refunded, has eliminated this risk for the future. To make the change, however, the state's General Fund spending will be restrained by pulling the accounting of the surplus forward a year by having to account for the \$113.6 million surplus collected in FY 2004-05 immediately instead of during the following year. Enactment of House Bill 03-1238 means that the required cuts to the General Fund in FY 2004-05 will be \$179.4 million rather than \$70.3 million as would have otherwise been the case. As the surplus continues to grow, the budget must similarly absorb the additional amount each year.

“The recent actions of the General Assembly to increase fee revenue in various cash funds will create larger TABOR surpluses.”

Impacts of cash fund increases. Since cash fund revenue is part of the TABOR limit, but the refund is accounted for in the General Fund, increases in cash fund revenue have a negative impact on the General Fund as they increase the amount of surplus revenue, and *vice-versa*. The recent actions of the General Assembly to increase fee revenue in various cash funds will create larger TABOR surpluses. Another factor that influences the TABOR surplus is higher tax rates to maintain the solvency of the Unemployment Insurance Trust Fund. While the higher tax rates are necessary, they will create larger TABOR surpluses that will be refunded from the General Fund. Given the expected General Fund budget shortfalls through FY 2005-06, the larger TABOR surpluses are at least partially responsible for the necessary budget reductions in the General Fund.

Table 9
June 2003 Forecast for the TABOR Revenue Limit and Emergency Reserve
(Dollars in millions)

	Actual FY 2001-02	Estimate FY 2002-03	Estimate FY 2003-04	Estimate FY 2004-05	Estimate FY 2005-06	Estimate FY 2006-07	Estimate FY 2007-08
TABOR Revenues:							
General Fund /A	\$5,519.8	\$5,315.7	\$5,534.0	\$5,911.0	\$6,343.1	\$6,756.9	\$7,186.2
Cash Funds	2,232.4	2,267.8	2,559.5	2,787.8	2,952.8	3,104.7	3,071.3
Total TABOR Revenues	\$7,752.2	\$7,583.5	\$8,093.5	\$8,698.8	\$9,295.9	\$9,861.6	\$10,257.5
LIMIT:							
Allowable TABOR Growth Rate	10.0%	6.9%	6.7%	6.1%	4.3%	4.8%	5.1%
Inflation	4.0%	4.7%	1.9%	2.0%	2.8%	3.0%	3.1%
Population Growth	6.0%	2.2%	1.7%	1.2%	1.5%	1.8%	2.0%
Population Adjustment for Growth Dividend (6% Carried Forward)		0.0%	3.1%	2.9%	0.0%	0.0%	0.0%
Allowable TABOR Limit	\$8,126.2	\$8,287.1	\$8,093.5	\$8,585.2	\$8,954.3	\$9,384.2	\$9,862.7
Revenues Above / (Below) TABOR Limit /B	-\$365.7	-\$703.6	\$0.0	\$113.6	\$341.5	\$477.4	\$394.7
EMERGENCY RESERVE:							
TABOR Emergency Reserve /C	\$232.6	\$227.5	\$242.8	\$257.6	\$268.6	\$281.5	\$295.9

Totals may not sum due to rounding.

Note: TABOR broadly defines spending such that expenditures are equal to revenues. The statutory 6 percent limit applies to the General Fund appropriations only. Thus, the two concepts are not directly comparable.

/A These figures differ from the General Fund revenues reported in other tables because they net out revenues that are already in the Cash Funds to avoid double counting. For instance, the General Fund gaming revenues are netted out. These figures also include the amount of sales and use tax, after the over-refund of surplus TABOR revenues. Senate Bill 97-1 diverts 10.355% of the gross sales and use tax revenues to the Highway Users Tax Fund under certain conditions.

/B Includes \$8.3 million in FY 2001-02 for understated revenue from a prior year.

/C In years where the projected revenues exceed the amount allowed by the Constitution, the reserve is calculated based on the limit, rather than on projected receipts. Given that the state will only retain the maximum allowed by the Constitution, it need only reserve three percent.

OVERVIEW OF THE ECONOMY

National Economy

This section provides a review of the recent performance of the national economy and details the national economic forecast.

Recent data. Inflation-adjusted gross domestic product (**GDP**) indicated that the economy grew by 1.9% in the first quarter. The national economy is growing beneath its full potential. Rising energy prices, fears over the war in Iraq, and falling business and consumer confidence led to the low growth rate in the first quarter. Still, the fact that the economy had growth surprised some economists who expected GDP to decline.

Employment is significantly lagging the slow recovery in the economy. Nearly 2.5 million jobs have been shed since February 2001, including almost 300,000 in the past four

months. Most of the recent job losses were in February and March because of uncertainty with respect to the war in Iraq. Employment was flat in April and 17,000 lower in May. Combined with an increase of 58,000 temporary services jobs in May, the worst of the employment losses may be behind us. An increase in temporary workers is typically a leading indicator for an expanding economy.

The **unemployment rate** has risen to a cyclical and nine-year high of 6.1%. In a positive note, announced layoffs in May were at the lowest level in 30 months, according to the Challenger Report. However, jobless claims have been above 400,000 for more than three months, a level that indicates a stagnant economy.



The **manufacturing** sector has been at recessionary levels for the past three months. When the Institute of Supply Management index is below 50, it indicates contraction for manufacturing. The manufacturing index took a positive turn in May, increasing to 49.4 from 45.4 in April. The new orders and production indices are expanding for the first time since February. The upturn in the index hopefully portends future expansion for the manufacturing sector.

“The manufacturing index took a positive turn in May...”

Since the first quarter, evidence is mounting that a more significant economic rebound is near. Since the quick victory in Iraq, **confidence** has been rising on three fronts. Each of the confidence factors will still take some time to work through the economy and will need to be sustained for a few more months to take full effect. *Investor confidence* is reflected in a rise in the major stock market indices. Since their mid-March lows, the NASDAQ has risen more than 25%, the S&P 500 index has increased nearly 25%, and the Dow Jones 30 Industrials has increased about 20%. Investors are increasingly confident about business profits and the ability of businesses to increase investment. Low interest rates are contributing to their confidence.

Business confidence has also increased since March. This will eventually be reflected in an increase in investment. The decline of business investment since late 2000 was the primary cause of the recession and low growth period since then. After the long period of reductions, there is some pent-up demand for business investment. Business needs for increased productivity will help spur new investment. Companies that had put off investment decisions at the beginning of the year because of the war

now feel more confident to proceed. The low interest rate environment certainly makes investment affordable. The return to corporate profitability will enable businesses to use internal cash sources. Finally, the stock market rally should engender more initial public offerings and venture capital funding activity for external cash sources. A return to more robust economic growth will depend significantly on renewed business investment at healthy levels.

Consumer confidence is also rebounding from its March low. Confidence in May was at an 11-month high although it receded somewhat in the preliminary June survey. While consumer spending will increase during the next several quarters, its growth rate will not exceed the robust rates of the late 1990s. Consumer spending has been keeping the economy afloat during the downturn, thanks largely to low- or zero interest rates. Thus, as opposed to pent-up demand for new business investment, consumer spending is largely spent-up. Wage growth for consumers is likely to remain stalled because of weak employment growth and the pressure on employers from rising benefit costs. The "wealth effect" from a rising stock market is not likely to immediately help consumer spending. Consumers are more likely to replenish their depleted portfolios resulting from the three-year bear market than spend their recent gains. Still, to the extent that consumer spending does increase, it will provide help for other sectors of the economy.

“...consumer spending is largely spent-up.”

Lower energy costs will also benefit the economy during upcoming quarters. Four of the last five national recessions have been linked to significant run-ups in oil prices. To the extent that the recent price spikes have abated, the risk of a double-dip recession was reduced. Natural gas and electricity prices are expected

to move higher in the near term, however. If natural gas supplies are not boosted before the next heating season, higher prices will deter business and consumer spending.

“A boost to consumer paychecks from the impending federal withholding changes and rebate checks ... provide a welcome respite from the restrained wage gains of recent periods.”

The recently enacted **federal tax cuts** will help spending. A boost to consumer paychecks from the impending federal withholding changes and rebate checks to taxpayers with minor children will provide a welcome respite from the restrained wage gains of recent periods. While some consumers will use the increased disposable income to reduce their debt levels rather than spend it immediately, it still sets up improved prospects for increased spending in the future.

The Federal Reserve Board is poised to act with even **lower interest rates** in the event that the economy does not show signs of renewed life or deflation poses a threat. Low interest rates have certainly sustained the economy, particularly the automobile and housing markets. They will continue to do so until other sectors of the economy strengthen. While much has been said about the impact of higher interest rates on the housing market, the timing and degree of the increases will be critical. If interest rates do not increase until 2004, the increases are relatively small and infrequent, and income gains become more solid, the housing market could escape significant damage.

The National Economic Forecast. This section presents the forecast of the national economy. The detailed forecast can be found in Table 10.

- Inflation-adjusted gross domestic product (**GDP**) will increase 2.3% in 2003. However, the first and second halves of the year will be very different. The economy will pick up in the second half of 2003 with growth rates of 3.6% in the third quarter and 4.1% in the fourth quarter. This strength will carry into 2004 when the economy is projected to expand by 3.7%. Growth will slow to 3.0% in 2005.
- Nonfarm **employment** growth will lag the overall expansion of the economy. On average, there will be 100,000 fewer jobs in 2003. In 2004, employment will finally begin to expand and growth will be 1.2%. More robust growth of 2.1% will occur in 2005. The **unemployment rate** will average 6.0% in 2003, following a jobless rate of 5.8% in 2002. The unemployment rate will begin to improve in 2004 and decline through the remainder of the forecast period.
- **Income** growth will remain muted this year. Employers are trying to hold down wage and salary gains because of rising benefit costs. Additionally, employers have the ability to constrain wage increases because of the weak labor market. These factors will begin to ease next year. Personal income will increase 3.7% in 2003, followed by 4.0% and 4.5% gains in 2004 and 2005, respectively.
- Record-low mortgage rates and a perceived stock-market alternative drove a 16-year high for **housing starts** in 2002. The cyclical high is above sustainable levels and will have to eventually return to more normal levels. Low mortgage rates again in 2003 will lead to another prosperous year for the housing market. Housing starts will decline by 0.8% this year, before they contract by 11.0% in 2004.

- **Inflation** will be relatively low in 2003, thanks to slight deflationary pressures for consumer goods. The services portion of the typical consumer market basket will somewhat offset the trend for goods. Additionally, high energy prices in the runup to the war in Iraq, as well as later in 2003 when a natural gas shortage is expected to increase its price, will counterbalance deflationary trends. Thus, inflation will be an estimated 2.5% in 2003, before declining to 2.1% in 2004. A rebounding economy, the fall in the dollar's value that increases the price of imported goods, and intervention by the Federal Reserve Board should keep deflation at bay.

While the economy seems poised to start down a stronger growth path, several **risks** remain for the forecast. If any of the several current positive *confidence* factors for the economy falter, the expansion would come to a halt. A combination of an economic slowdown and *deflation* could set off a deflationary and recessionary spiral. Substantial *further weakening of the dollar* could force the Fed to raise interest rates in support of the dollar at the risk of choking off the economy. Higher-than-anticipated energy costs would also endanger the expansion. *Higher natural gas prices* seem likely in the fourth quarter. While this forecast anticipates a 26% annualized increase at that time, an even larger increase would be damaging to the economy.

Table 10
National Economic Indicators, June 2003 Forecast
(Dollar amounts in billions)

	1999	2000	2001	2002	Forecast 2003	Forecast 2004	Forecast 2005	Forecast 2006	Forecast 2007
Gross Domestic Product (GDP) percent change	\$9,274.3 5.6%	\$9,824.7 5.9%	\$10,082.1 2.6%	\$10,446.3 3.6%	\$10,872.1 4.1%	\$11,439.1 5.2%	\$11,998.0 4.9%	\$12,641.4 5.4%	\$13,261.5 4.9%
Inflation-adjusted GDP percent change	\$8,858.9 4.1%	\$9,191.4 3.8%	\$9,214.5 0.3%	\$9,439.9 2.4%	\$9,657.0 2.3%	\$10,014.3 3.7%	\$10,314.8 3.0%	\$10,665.5 3.4%	\$10,985.4 3.0%
Nonagricultural Employment (millions) percent change	129.0 2.4%	131.8 2.2%	131.8 0.0%	130.4 -1.1%	130.4 0.0%	131.9 1.2%	134.7 2.1%	136.9 1.6%	138.6 1.3%
Unemployment Rate	4.2%	4.0%	4.8%	5.8%	6.0%	5.9%	5.4%	5.2%	5.2%
Personal Income percent change	\$7,786.5 4.9%	\$8,406.6 8.0%	\$8,685.4 3.3%	\$8,929.0 2.8%	\$9,258.0 3.7%	\$9,631.2 4.0%	\$10,069.1 4.5%	\$10,528.8 4.6%	\$10,999.2 4.5%
Inflation (Consumer Price Index)	2.2%	3.4%	2.8%	1.6%	2.5%	2.1%	2.5%	2.4%	2.3%
10-year Treasury Note	5.6%	6.0%	5.0%	4.6%	4.2%	4.7%	4.9%	5.8%	5.9%

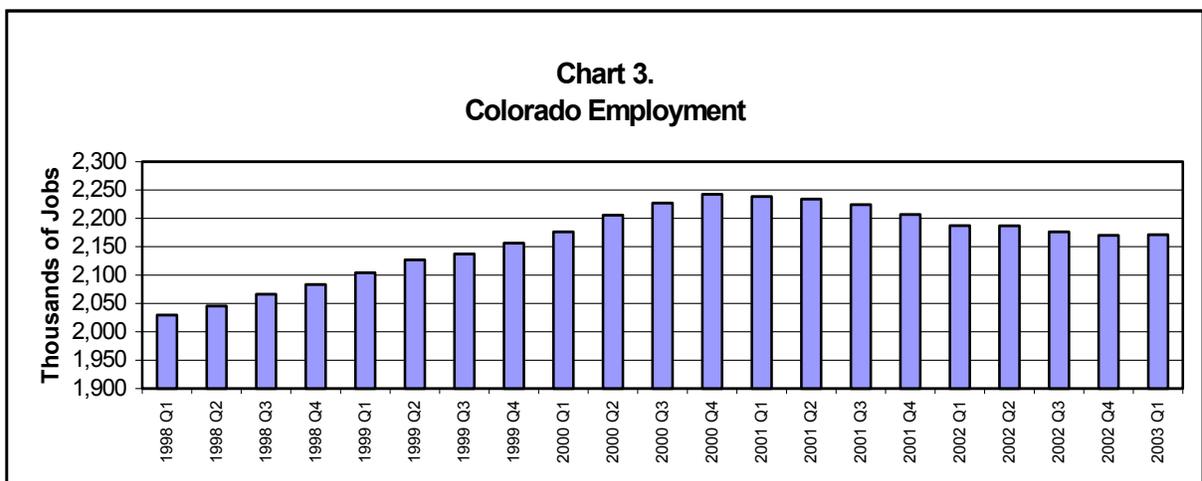
Colorado Economy

This section provides a review of the recent performance of the Colorado economy and the economic forecast for the state.

Recent performance. While most indicators suggest that Colorado's economy has reached the bottom point of the contraction, it is likely that it will remain there for much of 2003. Preliminary data indicates that employment decreased 1.9% in 2002, and Colorado lost nearly 43,000 jobs. Employment declined in every industry except mining and government. Job losses slowed to a trickle during February and March. On a seasonally adjusted basis, Colorado gained 4,000 jobs in April, the first gain in eight months. In addition, the employment services sector, which includes temporary workers, gained 1,500 jobs in April. This suggests that employment has hit the bottom of the business cycle because businesses tend to hire temporary workers before increasing their full-time work forces. However, the increase will need to occur for several more months before it can be firmly concluded that the recession has ended. Through April, the number of jobs was down 0.4% over a year ago. There were 81,000 fewer jobs in Colorado in April than during December 2000, the peak employment level prior to the recession.

The unemployment rate continues to edge upward. The unemployment rate averaged 5.3% in 2002 and 5.7% through the first four months of the year. It reached 6.0% in April, the highest level since January 1993.

In another sign that job losses have begun to ebb, the number of job gain announcements has begun to be more on par with the number of layoff announcements in recent months. Prominent layoff announcements have occurred in several sectors. Agilent Technologies, Inc. will lay off 800 people statewide to reduce operating costs. Advanced technology manufacturer Sanmina-SCI laid off 99 people in Fountain. Sprint will eliminate 500 positions in Aurora when it shuts its Internet-site management operation. Invesco Funds Group will lay off 125 people in July as it transfers the management of twenty funds to its sister company, Aim Investments. Finally, the Transportation Security Agency announced the reduction of 200 security screeners at Denver International Airport as part of a budget cutting move.



Job gain announcements occurred in the advanced technology, manufacturing, and food service sectors. Aerospace firm Raytheon Co. of Aurora announced plans to hire 200 systems engineers, software developers and computer scientists by the end of 2004. Advanced technology manufacturer Sirenza Microdevices Inc. is moving its headquarters to Broomfield from California in July along with 210 workers. Hunter-Douglas will open a tile manufacturing facility in Thornton and initially hire 50 people to staff it. The company eventually plans to add 2,000 jobs and build a 71-acre manufacturing campus on the site. Finally, Nobel/Sysco Food Services will hire 200 workers after it moves its office and distribution center from North Denver to Stapleton in late 2004.

“Aerospace firm Raytheon Co. of Aurora announced plans to hire 200 systems engineers, software developers, and computer scientists by the end of 2004.”

The weak employment situation was the primary influence on income growth in 2002. While wage and salary income declined 1.5%, transfer payments increased 10.9%. The primary driver for increases in transfer payments was unemployment insurance benefits, which increased 157.9%. Dividends, interest, and rent increased 1.4%. Total personal income increased 1.2%, a slower pace than that experienced in every state in the nation except New York. Per capita income decreased 0.5% in 2002, ranking last in the nation.

That personal income growth in Colorado was nearly the slowest in the nation during 2002 is another indicator that Colorado's economy may have reached its nadir. Just as Colorado followed the nation into recession, Colorado will follow the nation into recovery. Colorado's recession has also been deeper than that of the nation, so Colorado's recovery will

likely take longer than the nation's. Personal income growth in Colorado was the fastest in the nation as recently as 1999, and the second fastest in 2000. Colorado's employment growth was the third fastest in 2000. In 2002, the state ranked 49th in the nation for job growth. Colorado's recession was deeper than the nation's because it had a higher than average concentration in the advanced technology, telecommunications, airline travel, and tourism sectors. These sectors were those hardest hit by the national recession.

Spending has likewise been weak in Colorado. Retail trade decreased 0.7% in 2002 and is down 0.6% through the first quarter of 2003, compared with the same time period in 2002. In addition to general economic malaise, spending was adversely affected by the weak tourism season during 2002. The weak tourism season was caused by the national recession, the wildfires, and the drought. In addition, retailers have had little pricing power. Inflation increased only 1.9% in 2002 in the Denver-Boulder-Greeley area, the slowest rate since 1989.

“Colorado’s economy will bounce around the bottom of the business cycle for much of 2003.”

Colorado's economy will bounce around the bottom of the business cycle for much of 2003. Employment, wage, personal income, and consumer spending growth will be positive, but muted. Recovery in Colorado will depend on sustained growth in the national economy and the restoration of business and investor confidence.

The Colorado forecast. The following highlights summarize the Colorado economic forecast. The detailed Colorado economic forecast can be found in Table 11.

-
- Gains in employment will lag the recovery in other sectors of the economy. **Employment** will change little in 2003, increasing by slightly more than 2,000 jobs, or 0.1%. Substantive job gains will resume in 2004. Employment will increase 2.0%, or by about 44,000 jobs, and recover to pre-September 11, 2001 levels. Employment will increase 2.7% in 2005 and 2.9% in 2006. The unemployment rate will increase to 5.9% in 2003 before dropping to 5.6% in 2004, 5.2% in 2005, and 4.8% in 2006.
 - Income indicators will be weak, but positive, in 2003. After a 1.5% decline in 2002, **wage and salary income** will rise 1.9% in 2003. A weak labor market, business emphasis on profits, and the mix of job creation will restrict wage growth in 2003. More robust employment growth and larger raises will boost wage and salary income by 6.1% in 2004. After increasing 1.2% in 2002, **personal income** will increase 2.7% in 2003 and 5.4% in 2004. The growth rates in 2002 and 2003 are below the 4.5% threshold of Amendment 23, the funding mechanism for K-12 education passed in 2000. When personal income growth is below the threshold, the 5% maintenance of effort requirement for the General Fund may be waived. However, the overall funding level for education (inflation plus one percent plus enrollment growth) must be maintained so any decrease in General Fund effort would need to be afforded by the State Education Fund.
 - After a 0.7% decline in 2002, **retail trade sales** will increase 1.7% in 2003, still low by historical standards. Spending has continued to be weak through the first quarter of 2003. However, the apparent end of the drought in most areas of the state and the awakening economic recovery nationwide should result in a relatively healthier tourism season than in 2002. Spending will mirror income gains after 2003, remaining in the mid to high 5% range.
 - The number of **residential construction** permits issued will decrease 18.9% in 2003 after a 22.5% decrease in 2002. Multi-family housing construction is undergoing a correction following the construction boom in 2000 and 2001. Migration to the state is lower due to the weak economy and still high cost of living in Colorado relative to many other areas of the nation. Despite aid from low mortgage rates, this will depress single-family construction. Housing permits will decrease 8.8% in 2004 before increasing 3.9% in 2005.
 - **Nonresidential construction** will continue to correct from the boom years of the late 1990s in 2003, decreasing 31.7% after a 22.5% decrease in 2002. The high vacancy rates in office buildings will prevent significant activity in that sector. Significant retail construction will not occur because of weak consumer spending. Positive factors include several planned hospitals to address increasing health care needs and school construction approved by the voters. Nonresidential construction will not begin recovering until 2005.
 - The recession prevented prices from advancing in 2002, as the **inflation** rate was held to 1.9%, the slowest rate since 1989. The local inflation rate will remain low in 2003 at 2.0%. While energy prices will be high, the stagnant economy will afford little pricing power to retailers, wage pressure will be weak, and increases in housing prices will be muted.
 - The recession and Colorado's relatively weak economy relative to the rest of the nation has reduced migration to the state.

After increasing 1.7% in 2002, **population** growth in Colorado will slow to a 1.2% rate. The lower migration trends will hold through the next few years and eventually

subside as Colorado becomes more affordable relative to the rest of the nation. The state's population will increase 1.5% in 2004 and 1.8% in 2005.

Table 12
Colorado Economic Indicators, June 2003 Forecast
(Calendar Years)

	1998	1999	2000	2001	2002	Forecast 2003	Forecast 2004	Forecast 2005	Forecast 2006	Forecast 2007
Population (thousands), July 1 percent change /A	4,116.6 2.4%	4,226.0 2.7%	4,326.8 2.4%	4,431.0 2.2%	4,506.5 1.7%	4,560.6 1.2%	4,629.0 1.5%	4,712.3 1.8%	4,806.6 2.0%	4,902.7 2.0%
Nonagricultural Employment (thousands) percent change	2,057.0 3.9%	2,131.9 3.6%	2,212.9 3.8%	2,231.9 0.9%	2,189.0 -1.9%	2,191.2 0.1%	2,235.0 2.0%	2,295.4 2.7%	2,361.9 2.9%	2,432.8 3.0%
Unemployment Rate	3.8%	2.9%	2.7%	3.7%	5.3%	5.9%	5.6%	5.2%	4.8%	4.5%
Personal Income (millions) percent change	\$118,413 8.9%	\$128,386 8.4%	\$143,043 11.4%	\$148,239 3.6%	\$149,958 1.4%	\$154,048 2.7%	\$162,432 5.4%	\$171,312 5.5%	\$180,918 5.6%	\$191,414 5.8%
Wage and Salary Income (millions) percent change	\$69,604 11.3%	\$76,343 9.7%	\$86,048 12.7%	\$88,436 2.8%	\$87,069 -1.5%	\$88,701 1.9%	\$94,118 6.1%	\$99,774 6.0%	\$105,854 6.1%	\$112,397 6.2%
Retail Trade Sales (millions) percent change	\$48,131 6.6%	\$52,209 8.5%	\$58,018 11.1%	\$59,027 1.7%	\$58,634 -0.7%	\$59,631 1.7%	\$62,016 4.0%	\$65,427 5.5%	\$69,287 5.9%	\$73,444 6.0%
Home Permits (thousands) percent change	49.5 16.5%	48.9 -1.3%	53.7 10.0%	54.5 1.5%	47.9 -12.1%	38.9 -18.9%	35.4 -8.8%	36.8 3.9%	39.3 6.8%	40.1 2.1%
Nonresidential Building (millions) percent change	\$2,617 -12.4%	\$3,544 35.4%	\$3,339 -5.8%	\$3,373 1.0%	\$2,613 -22.5%	\$1,785 -31.7%	\$1,733 -2.9%	\$1,908 10.1%	\$2,070 8.5%	\$2,188 5.7%
Denver-Boulder Inflation Rate	2.4%	2.9%	4.0%	4.7%	1.9%	2.0%	2.8%	3.0%	3.1%	3.2%

/A Colorado's population on April 1, 2000, was 4,301,261 according to the U.S. Census Bureau. The changes that are shown in this table for 1998 to 2000 are based on the intercensal estimates by the Census Bureau and do not reflect the original estimates.