

NOTES TO THE TABOR SCHEDULE OF REQUIRED COMPUTATIONS

NOTE 1. PURPOSE OF THE SCHEDULE OF REQUIRED COMPUTATIONS

The purpose of the Schedule of Required Computations is to determine and document compliance with Title 24 Article 77 of the Colorado Revised Statutes, which is the implementing statute for Article X Section 20 of the State Constitution (TABOR). The report is required to include at a minimum state fiscal year spending, reserves, revenues, and debt. The schedule also includes a calculation of the limit on fiscal year spending, the amount required to be refunded or the amount of excess revenue retained by law, as well as all related adjustments.

TABOR has many provisions including a requirement for a vote of the people for new taxes or tax rate increases and a limit on the amount of fiscal year spending. Fiscal year spending is defined as district expenditures and reserve increases except those expended from exempt sources, such as, gifts, federal funds, damage awards, property sales, reserves, and other items. This definition, while focused on spending is essentially a limitation on revenue retention because reserve increases are unspent revenues. Therefore, the terms fiscal year spending and nonexempt revenue are used interchangeably throughout these notes.

The limit on revenue retention is based on an allowable growth percentage (See Note 12) applied to the lesser of the prior year's revenues or the prior year's limit. Revenues in excess of the limit are required to be refunded to taxpayers unless voters approve retention of the excess. In the 2005 general election, voters approved Referendum C, which allowed the state to retain revenues in excess of the limit for a five-year period (See Note 9 below).

NOTE 2. BASIS OF ACCOUNTING

Pursuant to Article 77 of Title 24, Colorado Revised Statutes, this report is prepared in accordance with generally accepted accounting principles (GAAP) for governmental entities except where an irreconcilable difference exists between GAAP, and state statute or the provisions of Article X Section 20 of the State Constitution (TABOR).

The accounting principles used by the State are more fully described in the State's Comprehensive Annual Financial Report available from the Office of the State Controller.

NOTE 3. DEFINITION OF THE DISTRICT

TABOR defines the district as "the state or any local government, excluding enterprises." It further defines enterprise as "a government-owned business authorized to issue its own revenue bonds and receiving under 10 percent of annual revenue in grants from all Colorado state and local governments combined."

The General Assembly, for the purpose of implementing TABOR, stated in C.R.S. 24-77-102(16)(a) that "state" means the central civil government of the State of Colorado, which consists of the following:

- (I) the legislative, executive, and judicial branches of government established by Article III of the state constitution;
- (II) all organs of the branches of government specified in subparagraph (I) of paragraph (a) of this subsection (16), including the departments of the executive branch; the legislative houses and agencies; and the appellate

and trial courts and court personnel;
and

(III) state institutions of higher education.

(b) "state" does not include:

(I) any enterprise;

(II) an institution or group of institutions of higher education that has been designated as an enterprise;

(III) any special purpose authority;

(IV) any organization declared to be a joint governmental entity.

The General Assembly has designated the following as enterprises excluded from the district:

- ◆ State Lottery,
- ◆ College Assist,
- ◆ CollegeInvest,
- ◆ Division of Wildlife,
- ◆ State Nursing Homes,
- ◆ Division of Correctional Industries,
- ◆ Petroleum Storage Tank Fund,
- ◆ State Fair Authority,
- ◆ Brand Board,
- ◆ Clean Screen Authority,
- ◆ Capitol Parking Authority, and
- ◆ Statewide Tolling Enterprise.

It further established a statutory mechanism that allows governing boards of the institutions of higher education to designate certain auxiliary operations as enterprises, which are also exempt from TABOR. Senate Bill 189 enacted in the 2004 legislative session, expanded the authority for each governing board of the state institutions of higher education to designate the entire institution as a TABOR exempt enterprise. The Board of Regents of the University of Colorado designated the entire University of Colorado as an enterprise during Fiscal Year 2004-05, and the remaining boards designated their institutions as enterprises in Fiscal Year 2005-06. The Auraria Higher Education Center Board of Directors did not designate

all of its activities as a TABOR enterprise, but it continues to have selected activities designated as a TABOR enterprise.

Although the General Assembly and governing boards have designated certain enterprises as exempt from TABOR, those enterprises must continue to meet the criteria of a government-owned business authorized to issue its own revenue bonds and annually receiving under 10 percent of its revenue in grants from all Colorado state and local governments combined. In Fiscal Year 2006-07 the State Fair Authority received more than ten percent of its annual revenue in a transfer from the Travel and Tourism Promotion Fund managed by the Governor's Office of Economic Development; therefore, it did not qualify as a TABOR exempt enterprise (See Note 14).

NOTE 4. DEBT

Certificates of Participation, which are used by the State for long-term lease purchases, are not considered debt of the State for purposes of this report as provided by C.R.S. 24-30-202(5.5).

In interrogatories submitted by the General Assembly regarding House Bill 99-1325, the Colorado Supreme Court ruled that Transportation Revenue Anticipation Notes (TRANS) issued by the Colorado Department of Transportation do not constitute debt of the State as defined in Article XI Section 3 of the State Constitution. However, the Supreme Court ruled that the TRANS are a multiple-fiscal year obligation as defined by Article X Section 20 of the State Constitution, thus requiring an approving election before issuance. In November 1999 the voters approved the issuance of \$1.7 billion of TRANS.

NOTE 5. EMERGENCY RESERVES

TABOR requires the reservation, for declared emergencies, of 3 percent or more of fiscal year spending, excluding bonded debt service payments. This requirement for FY 2006-07 totals \$289,256,007. At June 30, 2007, the financial net assets of the following funds were applied to the reserve, up to the limits set in the Long Appropriations Act:

- ♦ Major Medical Fund – The \$40,000,000 designation by the Legislature has been reduced by \$6,240,000 because that amount was transferred out of the TABOR emergency reserve to the Disaster Emergency Fund per Governors' Executive Orders to pay the cost of fighting wildfires and tornado damage mitigation in the state.
- ♦ Subsequent Injury Fund – \$40,000,000.
- ♦ Worker's Compensation Cash Fund – \$12,000,000.
- ♦ Wildlife Cash Fund – \$100,000,000. The Wildlife Cash Fund's net assets not invested in capital assets (net of related debt) total \$37,471,933. The remaining \$62,528,067 of the Wildlife portion of the reserve comes from the capital assets recorded in the Wildlife Cash Fund.

The 2006 legislative session Long Appropriations Act, as amended by the 2007 legislative session Long Appropriations Act, designated up to \$90,000,000 of state properties as the remainder of the emergency reserve. The estimate of the needed reserve was based on the December 2006 revenue estimate prepared by Legislative Council. Because the revenues subject to the TABOR reserve requirement were significantly more than estimated, the amount designated for the reserve was \$7,256,007 less than required by the State Constitution. There is no process by which the General Assembly can adjust the

designated reserve after the end of the legislative session when the total TABOR revenues are known. In the event of an emergency that exceeded the financial assets in the reserve, the designated Wildlife Cash Fund capital assets and general capital assets would have to be liquidated to meet the constitutional requirement.

NOTE 6. STATUS OF REFUNDING

When refunds are required they are distributed to individual state taxpayers based on statutory mechanisms as discussed in Note 16. The Department of Revenue makes the distributions of the TABOR refund through the income tax refund process using estimates of the number of taxpayers expected to qualify for the TABOR refund. Because the exact number of qualifying taxpayers cannot be known in advance, the estimates may result in over or under distribution of the required refund throughout the four-year period allowed for amended tax returns.

As required by statute, under distributions are carried forward to subsequent years and added to the required refund. Over refunds are also carried forward to subsequent years and are used to offset any future refund liability. The statute requires the over/under refund carry forward to be applied in the year following the year in which the refund is required to be made, which results in a two year lag between the recording of the excess revenue and the adjustment for over or under refunds of those excess revenues.

At the beginning of Fiscal Year 2006-07 the state had an outstanding TABOR refund liability of \$2,916,844 related to Fiscal Year 2004-05 nonexempt revenues in excess of the limit. At the end of Fiscal Year 2006-07, \$727,335 of that liability remained to be refunded. Because of late filed and amended tax returns, the state continues to refund the outstanding unrefunded balance for up to four years after the excess revenues are recorded.

Because Referendum C precludes refunds until Fiscal Year 2010-11, the unrefunded balance is being carried forward on the Schedule of Required Computations and will be added to the next refund that is required by TABOR and the related implementing statutes.

A suit was filed in state court challenging the constitutionality of \$442.7 million of transfers from various cash funds to the General Fund made in and after Fiscal Year 2001-02 to mitigate shortfalls of general-purpose revenues. The suit claimed that the transfers required increases or continuation of fees to replenish cash funds reserves, and these fees were actually tax increases not approved by the voters as required by TABOR. Plaintiffs seek to prevent similar future transfers, to terminate existing fees replenishing the cash funds, to prevent fee increases intended to replenish the cash funds, and to require the General Fund to replenish the cash funds. After Colorado Court of Appeals decisions, both the plaintiffs and the state petitioned the Colorado Supreme Court, and the case was accepted for review.

NOTE 7. OTHER SOURCES AND ADDITIONS

The \$423.2 million reported in this line item primarily comprises: \$310.8 million of pension and other employee benefit trust fund investment earnings and additions by participants; \$52.3 million of unclaimed property trust fund additions exempted from TABOR by C.R.S. 38-13-116.5; \$33.6 million of accounts payable reversions, reimbursements of prior year expenditures, and other miscellaneous exempt revenues; and \$7.0 million of local government expenditures recorded by the state as revenues and expenditures to meet grant matching-funds requirements.

Other Sources and Additions also includes \$3.9 million of capital lease financing and \$15.6 million from the Great Outdoors Colorado Trust Fund (GOCO) paid to the Department of Natural Resources and exempted by the GOCO Enabling Act.

NOTE 8. VOTER APPROVED REVENUE CHANGES

When state voters approve a revenue change, the resulting revenues are exempt from the TABOR limit on fiscal year spending. The following revenue changes were approved by voters:

- ♦ In the 1998 general election, voters approved a citizen-initiated law, C.R.S. 25-8-501.1 – Regulation of Commercial Hog Facilities, which instituted a permit fee. The State collected \$158,846 and \$180,292 from this exempt source in Fiscal Years 2006-07 and 2005-06, respectively.
- ♦ In the 2000 general election, voters approved a citizen-initiated amendment that added Section 14 to Article XVIII of the State Constitution. This amendment allowed the use of marijuana for medical purposes and authorized the Department of Public Health and Environment to charge a fee for the issuance of a permit for such purpose. The State recorded \$141,137 and \$89,948 including interest and unrealized gains/losses from this revenue source in Fiscal Years 2006-07 and 2005-06, respectively.
- ♦ In the 2000 general election, voters approved a citizen-initiated amendment that added Section 17 to Article IX of the State Constitution. This amendment created the State Education Fund and diverted the revenues from a tax of one-third of one percent on taxable income of individuals, corporations, estates, and trusts from the General Fund to the State

Education Fund. It also exempted the revenue from TABOR. The amendment was effective January 1, 2001 and resulted in \$409,497,995 and \$364,885,961 of tax revenues, interest, and unrealized gains/losses, being excluded from fiscal year spending in Fiscal Years 2006-07 and 2005-06, respectively.

- ◆ In the 2004 general election, voters approved a citizen-initiated amendment that added Section 21 to Article X of the State Constitution. The amendment authorized additional cigarette and tobacco taxes (3.2 cents per cigarette and 20 percent of manufacturer's list price for other tobacco products) effective January 1, 2005. The amendment specified the use of the tax revenue generated for specific health related programs, and it exempted the revenue from the TABOR limitations. The state recorded \$168,173,648 and \$171,112,571 of tax revenues, interest, transfers, and unrealized gains/losses from this exempt source in Fiscal Year 2006-07 and 2005-06, respectively.
- ◆ In the 2005 general election, Colorado voters approved Referendum C – a measure referred to the voters by the Legislature. The referendum allows the state to retain revenues in excess of the TABOR limit for a period of five years, and it states that the excess revenue retained qualifies as a voter approved revenue change. However, in order to determine the amount retained, the Schedule of Required Computations must include the retained amount as nonexempt revenue. Therefore the retained amount is not reported in this note as a voter approved revenue change.

NOTE 9. REFERENDUM C

Referendum C was placed on the ballot by the General Assembly and was approved by the

voters in the November 2005 election. It contained the following provisions:

- ◆ The state shall be authorized to retain and spend all revenues in excess of the limit on fiscal year spending after July 1, 2005, and before July 1, 2010 (five fiscal years). The authorization constitutes a voter approved revenue change.
- ◆ After July 1, 2010, the state is allowed to retain revenues in excess of the limit on fiscal year spending up to a newly defined excess state revenues cap. The excess state revenues cap is the highest population and inflation-adjusted nonexempt revenue amount in the period from July 1, 2005, to June 30, 2010, also adjusted for qualification and disqualification of enterprises. This provision effectively disables the ratchet down provision of TABOR during the five-year period. (The ratchet down is a term used to describe the TABOR provision that requires each year's base for calculating the limit to be the lesser of the prior year's revenues or the prior year's limit.)
- ◆ A General Fund Exempt Account is created within the General Fund to consist of the retained revenues for each fiscal year. The Legislature shall appropriate the moneys in the account for health care, education (including related capital projects), firefighter and police pension funding (for local governments), and strategic transportation projects.
- ◆ The Director of Research of the Legislative Council shall report the amount of revenues retained with a description of how the retained revenues were expended.
- ◆ The State Controller's annual report demonstrating compliance with the statutes implementing TABOR shall include the amount of revenues that the state is authorized to retain and expend.

The Schedule of Required Computations shows that the state retained \$1,308,040,131 and \$1,116,134,410 of excess revenues as allowed by Referendum C in Fiscal Years 2006-07 and 2005-06, respectively. Additional information regarding how the \$1.3 billion was expended can be obtained from the report prepared by the Director of Research of the Legislative Council and from the Management Discussion and Analysis section of the State of Colorado Comprehensive Annual Financial Report.

NOTE 10. DISTRICT RESERVES

District reserves are the cumulative fund balances of the state reported in the state's Comprehensive Annual Financial Report at the fund level rather than the government-wide level. District reserves therefore exclude capital assets, liabilities that are not recorded in governmental funds at the fund level (primarily long-term liabilities), and net assets of the TABOR enterprises. The majority of these fund balances are not available for appropriation due to legal and contractual restrictions.

NOTE 11. PRIOR-PERIOD DISTRICT FUND BALANCE ADJUSTMENTS

Although there were prior period adjustments of fund balance reported in the state's Comprehensive Annual Financial Report, none of those adjustments affected the state TABOR district fund balances.

NOTE 12. SOURCES OF TABOR GROWTH LIMIT

After adjustment for voter approved revenue changes, the allowable percentage increase in state fiscal year spending equals the sum of inflation and the percentage change in state population in the calendar year ending six months prior to the start of the fiscal year. Inflation is defined in C.R.S. 24-77-102(8) as "the percentage change in the consumer price index for the Denver-Boulder Consolidated Metropolitan Statistical Area For All Urban Consumers, All Goods, as published by the U.S. Department of Labor."

The Office of State Planning and Budgeting provided the 3.5 percent allowable growth rate, which comprises a 1.4 percent increase for population growth (calendar year 2005) and a 2.1 percent increase for inflation.

NOTE 13. SPENDING LIMIT ADJUSTMENTS

In Fiscal Year 2006-07, there were two types of adjustments made to the base before applying the 3.5 percent allowable growth rate as follows.

- ♦ The Fiscal Year 2005-06 Fiscal Year Spending Limit was decreased by \$64,268 to remove Fiscal Year 2005-06 nonexempt revenue recorded by state agencies that received payments from the State Fair Authority, which was disqualified as a TABOR enterprise in Fiscal Year 2006-07. This adjustment is necessary so that the revenue counted in the Fiscal Year 2005-06 Fiscal Year Spending Limit is comparable to the Fiscal Year 2006-07 Nonexempt District Revenues. Because the State Fair Authority is not a qualified TABOR enterprise in Fiscal Year 2006-07, payments received by state agencies from the State Fair Authority are internal to the state's TABOR district, and therefore, are

not counted against the Fiscal Year 2006-07 Fiscal Year Spending Limit.

- ♦ The Fiscal Year 2005-06 Fiscal Year Spending Limit was decreased by \$108,236 for the qualification of the Statewide Tolling Enterprise as a TABOR enterprise. Because the Statewide Tolling Enterprise qualified as a TABOR enterprise in Fiscal Year 2006-07 its revenues will not be counted against the Fiscal Year Spending Limit; in order for the two years to be comparable, the Statewide Tolling Enterprise's nonexempt revenues must be removed from the Fiscal Year 2005-06 Fiscal Year Spending Limit.

One adjustment was made to the Fiscal Year 2006-07 Unadjusted Fiscal Year Spending Limit (after application of the 3.5 percent allowable growth rate). The Fiscal Year 2006-07 Unadjusted Fiscal Year Spending Limit was increased by \$7,165,009 in order to make the disqualification of the State Fair Authority neutral in regard to measuring excess fiscal year spending. The State Fair was a qualified TABOR enterprise in Fiscal Year 2005-06, and therefore, its revenues were not counted in that year and were not reflected in the base (prior to this adjustment). The State Fair Authority's revenues are counted in Fiscal Year 2006-07 Nonexempt District Revenues because it was disqualified as a TABOR enterprise, and in order for the two years to be comparable, the State Fair Authority's Fiscal Year 2006-07 nonexempt revenues have been added to the base.

NOTE 14. ENTERPRISE QUALIFICATION AND DISQUALIFICATION

The TABOR amendment to the State Constitution specifies that qualification and disqualification of enterprises shall change the district base. In order to ensure

comparability between the base and current year nonexempt revenue, when an activity qualifies as an enterprise the base is reduced by the activity's prior year nonexempt revenue offset by revenue that would have been counted as nonexempt due to the activity's interaction with other state agencies. When a TABOR enterprise becomes disqualified, its current year nonexempt revenue is added to the base after application of the population and inflation growth adjustment and its prior year payments to other state agencies are removed from the base (before application of the allowable growth rate).

As discussed in Note 13 above, the Statewide Tolling Authority became qualified as a TABOR enterprise in Fiscal Year 2006-07 after having been disqualified in Fiscal Year 2005-06, and the State Fair Authority was disqualified as a TABOR enterprise in Fiscal Year 2006-07. The dollar amounts of the base adjustments related to these changes to the state's TABOR district are listed in Note 13.

The qualification and disqualification of TABOR enterprises affects the Computation of District Fund Balance Changes, which shows a net increase in fund balance of \$2,470,400. That change comprises a \$6,833,441 increase related to the disqualification of the State Fair Authority as a TABOR enterprise and a \$4,363,041 decrease related to the qualification of the Statewide Tolling Authority as a TABOR enterprise.

NOTE 15. TREATMENT OF ERROR CORRECTIONS UNDER REFERENDUM C

CRS 24-77-103.5 requires that errors in the amount to be refunded be corrected in the year that they are discovered. In Fiscal Year 2006-

07, there were no errors identified by the Office of the State Controller or state agencies. However, the \$2,871,444 of net understatement of prior year refunds that was reported on the Fiscal Year 2005-06 Schedule of Required Computations is being carried forward until Fiscal Year 2010-11 or the first following fiscal year in which the state is required to distribute a TABOR refund.

NOTE 16. FUTURE REFUNDS

In the 1999 regular session, the General Assembly enacted mechanisms to refund Fiscal Year 1998-99 and subsequent years' excess revenue. In succeeding sessions the General Assembly enacted additional mechanisms to refund the excess revenue. The mechanisms become active at different thresholds depending on the total amount of required TABOR refund. The thresholds are indexed to reflect the growth in Colorado personal income and are calculated by the Department of Revenue. The growth in personal income for the relevant years (2005 to 2006) was 7.029 percent. The mechanisms are as follows:

1. An earned income tax credit of 10 percent of the federal tax credit. This is available when the TABOR refund is \$76.3 million or more.
2. An income tax deduction for charitable contributions in excess of \$500 made by individuals who claim the standard deduction. The TABOR threshold is \$107.0 million; however, per statute the threshold is not applicable during the five years in which the state retains excess TABOR revenue because of the passage of Referendum C.
3. An income tax credit of the lesser of \$500 or 100 percent of non-reimbursed foster care expenses for foster parents. This is available if the TABOR refund is \$256.7 million or more.
4. A business personal property tax credit, which is available when the TABOR refund is \$259.0 million or more.
5. Interest, dividend, and capital gains exclusion up to \$1,200 for individuals and \$2,400 for couples for tax year 2000. See mechanism number 12 for an increase that was applicable to later tax years. The TABOR threshold is \$396.2 million.
6. An income tax credit through December 31, 2007 to health and dental care providers who practice in certain rural areas. The TABOR threshold is \$402.3 million.
7. An income tax credit that is a percentage of the federal child care credit. The TABOR threshold is \$409.4 million.
8. An income tax credit for contributions to the Institute of Technology. The TABOR threshold is \$449.2 million.
9. A 50 percent sales tax credit for the sale, purchase, storage, use, or consumption of tangible personal property used directly and predominantly for research and development in Colorado. The TABOR threshold is \$460.2 million.
10. A reduction in the annual registration fees for motor vehicles and a 25 percent reduction in the fees for trucks, truck tractors, and other vehicles. The TABOR threshold is \$465.9 million.
11. An income tax credit for contributions to high technology scholarships. The TABOR threshold is \$465.9 million.
12. An extension of mechanism number 5 changing the maximums to \$1,500 for individuals and \$3,000 for couples in interest, dividends, and capital gains excludable from state income taxes beginning January 1, 2001. The TABOR threshold is \$493.9 million.

13. A sales tax exemption for certain pollution control devices. The TABOR threshold is \$493.9 million.
14. A sales tax refund when the sales tax rate exceeds 0.01 percent and is imposed on new or used commercial trucks or other vehicles that are used in interstate commerce and have a gross weight of more than 26,000 pounds. The TABOR threshold is \$493.9 million.
15. An income tax credit for eligible agricultural value-added cooperatives. The TABOR threshold is \$513.5 million.
16. An income tax credit for the cost of health benefit plans not paid by the employer or deducted from the individual's federal adjusted gross income. The TABOR threshold is \$564.6 million.
17. An expansion of the capital gains modification to include capital gains realized in tax years beginning on or after January 1, 2001, as well as a reduction of the holding period from five years to one year. The TABOR threshold is \$607.1 million.
18. Any remaining amount is distributed to all full-year Colorado residents 18 years and older as a refund of sales taxes. When the refund is estimated to be under \$15 for each qualified taxpayer, an identical amount is refunded to each qualified taxpayer. When the sales tax refund is estimated to be over \$15 for each qualified taxpayer, a fixed amount is set for each of six tiers of federal adjusted gross income. The Department of Revenue calculates the amount of the individual refund for each tier as a statutory percentage of the total sales tax refund divided by the number of anticipated taxpayers in each tier.

Due to the passage of Referendum C, there is no refund in Fiscal Year 2006-07, and therefore, none of the refund mechanisms discussed above are active.