

AN ANALYSIS OF COLORADO'S PROPOSITION 103

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EXECUTIVE SUMMARY

Colorado's Proposition 103 will raise state taxes \$532 million in the first year and about \$2.9 billion in the first five years.¹ It proposes to raise the income tax rate on individuals and families, as well as small businesses, and simultaneously to raise the state sales tax rate.² Proposition 103 is the only state issue on this fall's ballot.

Although Proposition 103 says the money will be spent for education, there is no guarantee that it will. Income taxes and state sales taxes are placed into the State's general fund, with few exceptions.³ Since there is no segregated funding mechanism for this tax increase, any new funds would go to the general fund to be spent as the legislature chooses. The measure is silent about reporting or accountability.

Proponents in presentations and debates characterize the changes as a "rollback" to 1999 levels, but taxes were higher then. At the time, the economy was strong and growing rapidly, so state taxes were raising revenues faster than the State could spend them under the limitations of the Taxpayer's Bill of Rights (TABOR).⁴ Automatic annual increases of growth in population and growth in the price level (inflation) were less than the set rates were raising, and over-collections were mandated to be returned to taxpayers. Rather than continue to collect more than allowed, the legislature

eventually matched rates with normal growth. For most people, the term "rollback" conjures images of retailers cutting prices from some higher level to a lower sales

price. The "rollback" in this situation would be a return to much higher levels found in earlier years under different circumstances.

This measure states that the tax increase is only "temporary," meant to sunset after five years. It would be in effect from January 1, 2012, until December 31, 2016. If there is no long-term, dependable stream of income to support a larger base of operations, then good management practices indicate that temporary funds be used only for "one-time" moneys, such as constructing a permanent facility. The availability and intent for the use of the funds appear destined for daily operations of the government. If the system grows dependant on the availability of the funds, then how will the system adapt to reverse the rate increase after five years? Is it realistic to imagine the tax hike will be eliminated?

THE PROCESS

People were initially exposed to the proposal as "Initiative 25," before it qualified for the ballot. That term is for the same concept in Proposition 103. The different identities merely reflect different points in its development. The proponent, Rollie Heath, a state senator from Boulder, raised the idea informally in the Senate, but did not receive sufficient support. No proposal was offered in the House of Representatives, which holds a slim Republican majority. The backers of the measure collected about 16,000 signatures from volunteer gatherers, and expended \$151,000 to paid petition gatherers to obtain another 127,000 signatures from registered voters.

PROPOSITION 103 ANALYSIS

SIZE OF TAX INCREASE

Proposition 103 increases income tax rates by 8 percent for individuals and corporations. The rate would rise to 5 percent from the current flat rate of 4.63 of adjusted gross income. This figure is defined on the federal income tax forms: Form 1040 for individuals and Form 1120 for corporations.

The proposal also asks to raise state sales tax rate by 3.4 percent over current levels, from its current 2.9 percent to 3.0 percent. State sales taxes are applied to most sales of finished goods. The broadest exceptions are for food and medicines. The new, higher sales tax rate would be applied to services such as monthly telephone and energy bills, which are already taxed.

A PECULIAR ELECTION DAY

Popular and business calendars, and electronic day-minders list a standard election day across the nation. Colorado's TABOR elections, however, occur on the "first Tuesday in November of odd-numbered years"⁵ rather than the first Tuesday after the first Monday that most people expect. The consequence is that the statewide ballot for Proposition 103 will be voted on November 1. Sixty of Colorado's 64 counties will have only mail-in ballots⁶, so most voters should place their ballots in the postal system no later than October 28 to ensure timely delivery.

WILL ALL THE NEW FUNDING GO TO EDUCATION?

The measure calls for "additional revenues resulting from these increased tax rates [to] be spent only to fund public education from preschool through twelfth grade and public postsecondary education"—that is, K-12 government schooling, government preschools and state higher education institutions. Proponents present the tax increase in this fashion and base their arguments on it.⁷

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The proponents establish *intent* only. Proposition 103 does not create a segregated, separate fund. There is no basket into which the new money figuratively will be dropped. There are no specific instructions, nor any requirement for accountability or reporting. A loose statement of intent will not provide officials within government the specific guidance, such as was provided in Amendment 23. People of good will undoubtedly are going to disagree about how to implement the issue if the measure passes. As occurred with Referendum C, unanticipated adjustments are probable.

Let's do a thought experiment to demonstrate likely circumstances.

What if the economy continues to recover and taxes go

up \$630 million, even more than predicted? Could an argument be made that it was a combination of higher rates and more economic activity? How much of each? Could one argue instead that it was all due to higher rates? Or mostly due to the better economy? The legislature could employ dollars elsewhere and argue other forces are at work.

What if instead the economy slows and taxes do not raise the extra \$532 million projected? Do *all* increases from the previous year have to go to the School Finance Act?

Not one of these answers is clear now, and in the chaos of legislative negotiation and budget-setting, likely will be more muddled. The legislature may direct its staff to come up with a formula to direct any tax receipts above last year's base. Because Proposition 103 specifically requires that "... additional tax revenues be in addition to and not substituted for..." existing funding, the formula probably will mandate that funding be at least as large as the prior year's. But Amendment 23 already does that.

Finally, the language changes statute, not constitutional provisions. This legislature or the next (post-2012 election) could simply pass a new law to eliminate the education provision.

WHAT DO STUDIES SHOW ABOUT THE EFFECTS OF PROPOSITION 103?

There has been general agreement among economists and other public policy participants over years, that it is dangerous to raise taxes at the wrong time. A strong argument is commonly repeated that moving money from the productive, voluntary sector—that is, taxing the private sector even further at any time—serves to reduce total output. Higher taxes on businesses mean less money to hire new employees, or to pay higher wages and benefits. The general agreement is strengthened during a recession, or as an economy is struggling to emerge from an economic trough. President Obama repeated that message in a 2009 NBC News interview.⁸

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Barry Poulson, a retired Economics Professor from the University of Colorado at Boulder, observed the estimates of the cost to the taxpayer were generated at the Capitol as if people ignore the disincentives of higher taxes. Using an econometric model that attempts to capture how taxpayers respond, he and Dr. James Merrifield found that real costs could be as much as double those derived by Legislative Council staff's less sophisticated static analysis. Additionally, Poulson and Merrifield predicted a direct reduction of up to 11,600 jobs.¹⁰ By way of comparison, the Business Research Division at CU-Boulder's Leeds School of Business predicts that the Colorado

economy will generate only 25,000 total new jobs for all of calendar year 2011.¹¹

IS PROPOSITION 103 THE ONLY ENHANCEMENT TO EDUCATION FUNDING?

It is critical to remember the context in which the proponents call for higher funding, especially for education.

The state legislature funds K-12 education with the School Finance Act in the current budget year at \$6,545 per pupil.¹² Many school districts augment that with local mill-levy overrides. A total for operating expenditures which would encompass additional state spending (including categorical funding), as well as mill levy overrides and federal programs, brings Colorado's annual per-pupil spending to \$9,631, according to the most recent data.¹³

Amendment 23 is still in operation, 11 years after passage. This year, it will add \$384 million to the State Education Fund.¹⁴ Additional funds generated during the fiscal year that ended June 30, 2011, will add \$295 million beyond that amount.¹⁵

In 2005, voters approved Referendum C, which allowed the State to retain for five years an unlimited collection of taxes, based on the then-current tax rates. The result was that the State has a new, higher base on which to grow the budget. This year, Referendum C dollars will add \$927 million to collections by the State over what would have

been taxed in its absence.¹⁶

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HOW WILL INCREASED FUNDING AFFECT EDUCATION?

Proponents of the tax increase have not explained why more funding will solve problems. In fact, the problem is never defined except as there being too little money for education. Even with annual increases in the state per-pupil expenditure, student performance results have stayed stubbornly stagnant.

Across the nation, Americans have increased spending on K-12 education by 50 percent over the past 30 years, and doubled spending over the past 40 years. Educational outcomes, as defined by test scores and international comparisons, have barely budged. Some school districts such as those in Washington, D.C., and New York City spend the highest amounts per pupil and have worse outcomes than Colorado's test scores. The neighboring state of Utah spends \$2,700 per pupil less than Colorado and enjoys better outcomes (see below).

Colorado arguably has created successful reform for school choice, but only within government school networks. Through open enrollment students may attend schools outside their matriculation boundaries, if room can be found. Charter schools are permitted and in most cases, even thriving. There are many examples throughout our state of government schools structured to meet special programs or needs such as learning trades, being challenged in a core knowledge college preparatory, or high schools for pregnant teens or single mothers. Attempts at broader reforms, however, such as universal vouchers, vouchers for at-risk students, or educational tax credits, have all been stopped cold.

HOW DOES COLORADO COMPARE IN EDUCATION FUNDING?

An issue raised frequently at discussions of Proposition 103 is that Colorado funds education very poorly; that the

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State is “49th in the nation.” A separate claim is that the State “ranks 40th in per pupil spending.” The information presented is disingenuous at best, and blatantly wrong, at worst. Even the national teacher’s union places Colorado at 30th ranked spending in the nation.¹⁷

The first allegation is based on observing the relative wealth of Colorado’s citizens, as measured by personal income rankings. Statistically, the easiest way to perform better, then, is for residents to become poorer. Such analysis says nothing about the cost and reasonableness of service delivery.

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A national average of per-pupil funding explains little, because it pulls into the calculation high-cost, low-results places such as New Jersey and New York. A reasonable comparison is with surrounding states or other Rocky Mountain States.¹⁸

Total spending per pupil, which includes annual operations plus construction and debt financing shows Colorado spent \$11,133 per year in 2007-08.¹⁹ Kansas spends \$112 less and New Mexico \$324 less per year. Arizona is \$1,442 lower than our state and Utah \$3,200. Locally, only Nebraska comes in higher, at \$1,164 more.

Let’s also look at the most recent figures, for the 2009-10 school year, compiled by the national teachers union. We see that Colorado spends \$9,631 per pupil for daily operations only²⁰, as a statewide average for each child for each year. New Mexico and Nebraska are higher, by \$1,181 and \$129, respectively. Kansas, Oklahoma and Utah are lower, by \$367, \$1,663 and \$2,772, respectively. This puts Colorado in the middle-of-the-pack or a little ahead when making regional comparisons of per pupil spending.

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ENDNOTES

- ¹ Colorado Legislative Council staff, as stated in the ballot language.
- ² The State of Colorado imposes a sales tax on goods at final sales. Cities, counties and special districts (such as the Regional Transportation District and the stadium district in the Denver area) impose additional rates, commonly bringing a combined sales tax rate to 7 percent or even 8 percent. Over-rides of Taxpayer Increment Financing (TIFs), which are used to subsidize planned developments, act as additional sales taxes in specific locales.
- ³ Colorado Constitution, Article IX, Section 17 (Amendment 23) directs that the first 0.33 percent of income taxes be directed to the State Education Fund. Article XXIV directs the first 85 percent (until fully funded) of states sales tax to the Old Age Pension Fund.
- ⁴ For more information about the Taxpayer's Bill of Rights, see "Celebrating TABOR" on the Fiscal Policy pages of the Independence Institute web site (<http://tax.i2i.org/celebrating-tabor/>).
- ⁵ Colorado Constitution, Article X, Section 20 (The Taxpayer's Bill of Rights), paragraph (3)(a).
- ⁶ Colorado Secretary of State. "2011 County Election Methods." <http://www.sos.state.co.us/pubs/elections/vote/2011CountyElectionMethods.png>
- ⁷ See Great Education Colorado web site (<http://www.greatedaction.org/what-does-the-heath-initiative-do/>). See also Bright Colorado web site (<http://voteyeson103.com/index.php?id=3>)
- ⁸ <http://www.youtube.com/watch?v=PwoKOFgghxl&feature=related>.
- ⁹ Eric Fruits. "Tax Policy and the Colorado Economy: The Effects on Employment and Migration."
- ¹⁰ Barry W. Poulson and John D. Merrifield. "Prop 103: What Is The Cost To Colorado Taxpayers?" <http://liberty.i2i.org/2011/10/03/proposition-103-what-is-the-cost-to-colorado-taxpayers/>.
- ¹¹ Richard Wobbekind, Associate Dean, at luncheon presentation for the Denver Association of Business Economists, September 21, 2011.
- ¹² Colorado Department of Education, Public School Finance, Fiscal Year 2011-12 School Finance Act Funding, <http://www.cde.state.co.us/cdefinance/SchoolFinanceFundingFY2011-12.htm>.
- ¹³ National Education Association, *Rankings of the States 2010 and Estimates of School Statistics 2011* (December 2010), pg. 55, Table H-11, http://www.nea.org/assets/docs/HE/NEA_Rankings_and_Estimates010711.pdf.
- ¹⁴ "Focus Colorado: Economic and Revenue Forecast," Colorado Legislative Council Staff Economics Section, September 20, 2011, found at (<http://www.colorado.gov/cs/Satellite?c=Page&childpagename=CGA-LegislativeCouncil%2FCLCLLayout&cid=1251599785318&pagename=CLCWrapper>), Table 1, "September 2011 General Fund Overview", line 28 "Addendum: Amount Directed to State Education Fund Per Amendment 23," page 4.
- ¹⁵ Ibid. line 29 "Addendum: Amount Directed to State Education Fund Per SB 11-156 and line 30 "Addendum: Amount Directed to State Public School Fund Per SBI 1-230."
- ¹⁶ Ibid, "Table 4 History and Projections of Revenue Retained by

Referendum C," page 8.

¹⁷ Nat. Educ. Assoc., *Rankings and Estimates* (December 2010).

¹⁸ Wyoming is not included in our comparison. The state's entire population is less than Colorado's El Paso County or Jefferson County. Besides its rural nature, its education funding comes from energy exploration and development and is paid by severance taxes that are exceedingly high on a per capita basis.

¹⁹ US Dept of Education (<http://www.scribd.com/doc/34549638/NCES-2007-08-Total-Spending-Per-Pupil>)

²⁰ Nat. Educ. Assoc., *Rankings and Estimates* (December 2010).