

STATE OF COLORADO

EXECUTIVE CHAMBERS

136 State Capitol
Denver, Colorado 80203-1792
(303) 866-2471



Bill Owens
Governor

November 12, 2002

Senator Dave Owen, Chairman
Joint Budget Committee
200 E. 14th Ave., 3rd Floor
Denver, CO 80203

Dear Senator Owen:

I submit to you a budget for FY 2003-04 that keeps spending in check, is consistent with available revenues, and invests in essential priorities for the people of Colorado.

This budget is submitted in a very difficult fiscal environment. As you are aware, the national recession and the events of September 11th caused our revenues – and those of 42 other states – to drop significantly (Graphs 1 and 2). For FY 2001-02, revenues in Colorado dropped 13 percent (Graph 3). We expect very modest revenue growth: 2.6 percent in FY 2002-03 and 6.2 percent in FY 2003-04; therefore, I am proposing a General Fund budget with an increase of only 2.7 percent.

Despite these tough fiscal times, I am proposing funding in areas that are priorities or are required per statute. Departments with the strongest growth are Public Health and Environment (up 15.9 percent) and Corrections (up 7.5 percent). The largest decrease is in the Governor's Office (down 4.8 percent). Table 1 displays the proposed departmental budgets for the executive branch. Included in the proposed budget are the following:

- The budget boosts K-12 total program education spending by 5.3 percent, or nearly double the average increase for the overall budget. For the fifth consecutive year, we funded education for the increase in inflation and enrollment, a commitment that I began prior to the passage of Amendment 23. In addition, one percent is added per the provisions of Amendment 23.
- To protect the people of Colorado and the men and women who work in our prisons, the Department of Corrections budget is increased 7.5 percent from the appropriation, or 12.3 percent after adjusting for the four percent reductions now underway.
- To adequately reflect what I consider to be appropriate funding levels, this budget restores \$4 million of the Tony Grampsas grants in the Department of Public Health and Environment. These grants are intended to help youths at risk of school failure or criminal behavior. As you will recall, I vetoed \$7.6 million of these funds last May. Because the law does not allow me to partially reduce line items, I had to eliminate the entire line. I would have preferred merely lowering the amount instead of eliminating it. Hence, the FY 2003-04 budget reflects a partial restoration of the funds.

- A \$1.6 million increase for the developmental disabilities (DD) program to provide services to 50 additional citizens. In total, funding for DD programs will increase \$6 million. Overall, the budget provides services to more than 7,100 developmentally disabled clients.
- A \$1.7 million increase for child welfare funding.
- A \$3.6 million increase of total funds (no General Fund) for caseload growth and cost of living increases in aging services programs.
- \$68 million to fund salary survey and performance awards for state employees.

As we begin the work of crafting the budget for the upcoming year, many challenges remain. Slow revenue growth, reliance on \$1.2 billion of one-time money to fund ongoing expenditures, and a FY 2003-04 budget bill that increased appropriations by more than 7 percent all contribute to a difficult financial environment this year. As a result, we are faced with lowering appropriations by \$550 million to ensure a balanced budget as required by the state's Constitution for the current year. I have already taken action to lower this year's appropriations by \$220 million. This leaves \$330 million that we must still reduce. I implemented the following measures to achieve the \$220 million:

- ✓ I vetoed roughly \$46 million out of the state's budget bill; of which \$45 million was General Fund;
- ✓ I required all agencies except K-12 education's total program and categoricals, developmental disabilities, and the School for the Deaf and the Blind to reduce expenditures by 4 percent of their FY 2002-03 General Fund appropriations;
- ✓ I required departments to eliminate General Fund increases in provider rates;
- ✓ I froze capital projects in their early stages of construction, a \$30 million savings;

In addition, I implemented the following measures to shore up the General Fund:

- ✓ The full amount of funds available were transferred in FY 2002-03 per House Bills 02-1445 and 02-1478 (\$223.9 million); and
- ✓ We required agencies to revert funds in FY 2001-02. These reversions totaled \$23.9 million.

Even after these actions, we still must come up with another \$330 million to \$388 million. I have thought long and hard about how to do this. In all the reductions taken to date, we have been careful to minimize the impacts on state citizens and services. In fact, while other states are slashing services and doing massive layoffs, this has not happened in Colorado. For example, California laid off 7,000 state employees; Iowa furloughed 50,000 workers; and Massachusetts,

Missouri, and Nebraska have eliminated Medicaid coverage for some families. Colorado has weathered this budget shortfall with relatively few layoffs or service reductions to citizens. This philosophy has guided my thoughts on future budget reductions.

Below, you will find my proposed plan to balance the budget over the next two fiscal years. In total, I am proposing budget savings of \$478 million in the current fiscal year. If adopted, these actions will balance the budget in the current year and next year. The key to solving this problem is to aggressively lower this year's appropriations base. By doing this, we assure that the budget shortfall will not grow nor will it be pushed out into subsequent years when it becomes more difficult to remedy. Table 2 details these reductions for your information. Many of these budget proposals will require statutory changes and I look forward to working with you on these solutions. The proposals are outlined as follows:

- ✓ Delay the payback of the controlled maintenance trust fund by one year to \$138 million in FY 2004-05 and \$138 million in FY 2005-06;
- ✓ Reduce the transfer to the capital construction fund to \$5.3 million from \$100 million in FY 2003-04;
- ✓ Shift the pay date for state government employees by one day. This will save the state \$268 million in total funds (\$134 million General Fund). This will also benefit employees because they will have one less month of reported income for the 2003 calendar year, but the pay date is only shifted by one day. Assuming a 33 percent tax bracket (including federal and state taxes), this saves state employees \$88 million in taxes. By implementing this policy, the state would prevent at least 2,300 layoffs.
- ✓ Maintain the state share of K-12 total program funding at \$2.5 billion, as is currently in the budget. This represents a \$225 million increase in FY 2002-03. However, I propose to change the mix of state funds that are used. The current General Fund appropriation for K-12 increases 7.5 percent (or \$155 million). I propose that we maintain the current level of state support for K-12 funding, but shift \$51 million of General Funds into the State Education Fund. General Fund commitment would grow 5.0 percent instead of 7.5 percent, which is currently in the budget.
- ✓ Require all Departments except Corrections and Medicaid to reduce expenditures by *an additional* 6 percent in FY 2002-03. Medicaid would be required to do only an additional 3 percent reduction. Corrections would not have any additional budget cuts. As has been the case in previous budget reductions, K-12 total program, K-12 categoricals, developmental disabilities, and the School for the Deaf and the Blind would be exempt. These are in addition to the 4 percent restrictions already put in place. These additional reductions will total \$143 million and will carry forward into FY 2003-04.
- ✓ I ask other departments outside of the executive branch to enact similar common-sense limitations on their spending. The courts, legislative, State, Treasury, and Law Departments all should enact the same reductions. I call on all departments outside of the executive branch

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to match the ten percent reduction taken by the executive branch in the current year and to increase next year's budget by the average for the rest of the state departments. By enacting a 10 percent cut in the current year, these departments could save \$27 million. If Judicial were to lower its FY 2003-04 budget from the 6.5 percent increase requested to the average 2.7 percent for the overall budget, the state would save \$8.7 million.

- ✓ Halve the tobacco cessation and research grants from the Tobacco settlement in FY 2002-03 and FY 2003-04 and send the tobacco money to the General Fund. This brings in \$11.5 million per year. Funding from the tobacco settlement for the visiting nurses, the Children's Basic Health Plan (CHP+), Prenatal Care through CHP+, Read to Achieve, Prevention Programs, and the Veterans' Trust Fund would remain fully funded.
- ✓ Enact some cash fund transfers and refinancings, totaling \$120 million in FY 2002-03 and \$14 million in FY 2003-04.
- ✓ Other smaller measures include: elimination of fleet replacements paid with General Fund; delaying by one month the deduction of medical insurance costs; and drawing down federal dollars by matching local funds in Human Services.

I look forward to working with you in a proactive manner in solving this budget shortfall. In my September 20, 2002 letter to your committee I asked for you to join me in crafting appropriate spending levels and in identifying specific areas to cut in order to assure a balanced budget as required by the State Constitution. I continue to welcome your input on constructive ways to balance the budget. More detailed discussions of the proposed FY 2003-04 budget are summarized in the attachment.

Sincerely,


Bill Owens
Governor

Summary of the FY 2003-04 Budget

K-12 Education

- K-12 Education funding remains a high priority for my administration. For the fifth consecutive year, my budget fully funds K-12 education for inflation, something that had not been accomplished in the decade prior to my administration. Funding for inflation and enrollment will come from sources other than the State Education Fund, including an \$85 million increase from the General Fund.
- An additional one percent above inflation and enrollment is included as per the requirements of Amendment 23 (\$42.3 million). Most of this funding comes from the State Education Fund.
- State spending on K-12 total program will increase 5.3 percent.
- Over the four-year period from FY 1998-99 through FY 2002-03, state spending on K-12 education increased by \$746.3 million, while state and local spending combined increased by more than \$1 billion. State spending on K-12 education has increased by more than 12 percent above inflation and enrollment growth during this four-year period.
- K-12 education comprises 41 percent of the General Fund (Graph 4).
- K-12 total program, categoricals, and the school for the deaf and the blind have been held harmless from budget reductions.
- Includes \$28 million of funding for K-12 school capital construction needs from the State Education Fund. This includes \$8 million for charter schools.

Health Care Policy and Financing

- Medicaid comprises just over 20 percent of the state's General Fund budget and has more than tripled since 1990.
- In the current budget request, approximately \$76 million in new General Fund is "No Choice" base growth for Medicaid caseload. Indeed, as shown in Graph 5, we are anticipating that Medicaid caseload will increase 8.2 percent in the current year and then another 5.4 percent in FY 2003-04. After decreasing for six years, Medicaid caseload posted an increase in FY 1999-00 and has since been on an upward trend. In FY 2003-04, we expect that all of the increase in Medicaid costs is attributable to caseload increases.
- Overall, the Medicaid budget proposes a 4.0 percent increase in General Fund spending from the original appropriation base and an 8.0 percent increase in General Fund from the base adjusted for the 4 percent reductions underway.

- Funding for the Children's Basic Health Plan (CHP+) will increase \$12.4 million. The restructuring of this program that I initiated two years ago caused an enrollment increase of 74 percent in the last two years.
- The Department is in the process of implementing three new programs for low-income households in the state:
 - ◆ During the 2002 legislative session, Governor Owens proposed and the General Assembly approved \$25.8 million in funding to extend prenatal care under CHP+. As a result, uninsured women age 19 and over, whose income is less than 185 percent of the federal poverty level, will be eligible for critical prenatal care to protect both the mother and the child. The Department projects that it will serve 2,900 women this year.
 - ◆ In February 2002, the Department implemented a dental benefit for CHP+ children. Through the Delta Dental provider network, eligible children have access to over 700 providers across the state. The comprehensive service package allows each child to receive critical preventative dental care.
 - ◆ Provision of treatment for breast and cervical cancer to low-income women earning less than 250 percent of poverty income. We expect 71 women to receive this treatment this year.

Higher Education

- Higher Education comprises 12.8 percent of the General Fund budget.
- The FY 2003-04 budget requests a 2.4 percent increase for enrollment funding relative to the appropriation adjusted for the four percent cuts.

Human Services

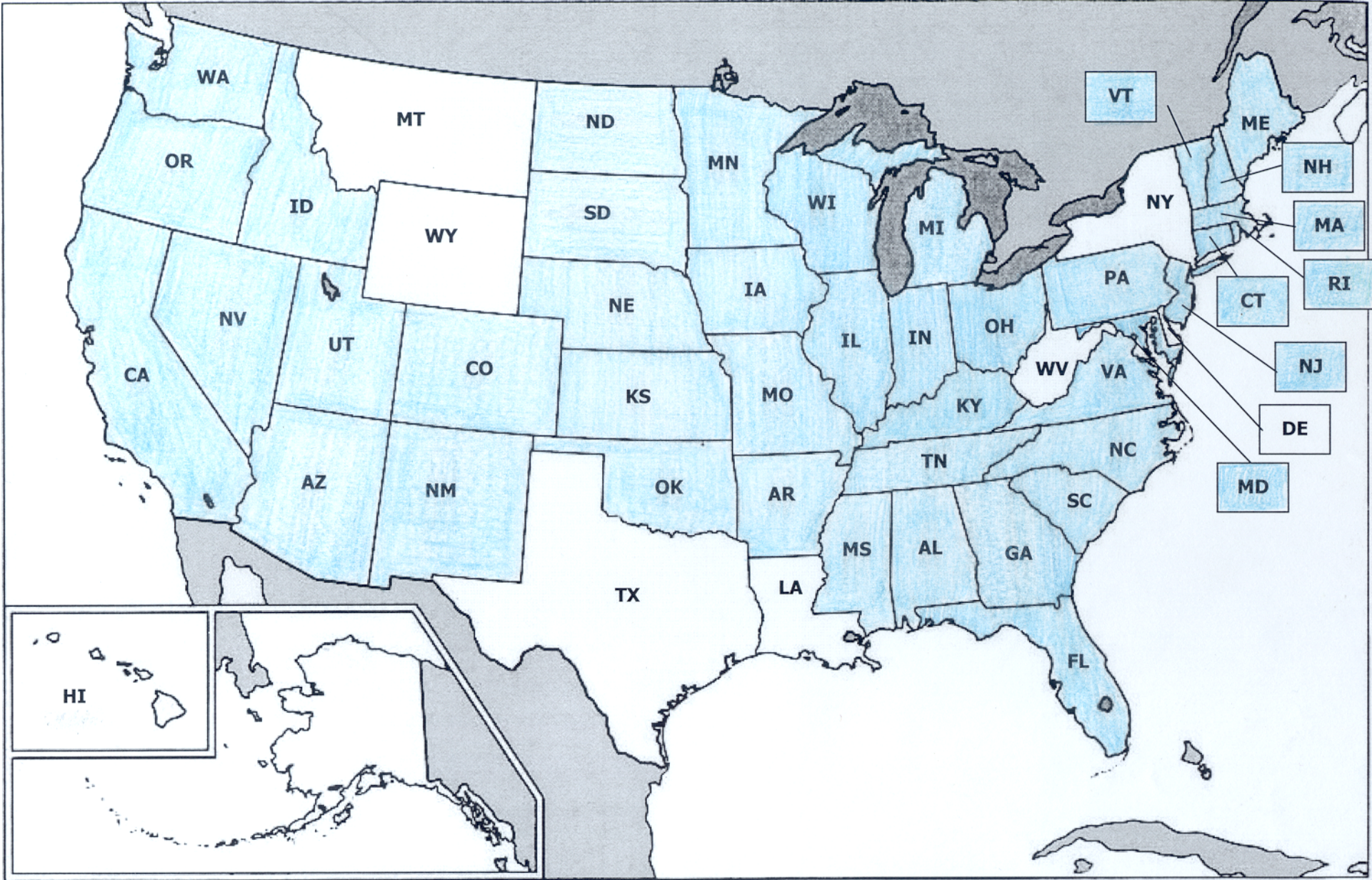
- Human Services comprises 8.8 percent of the General Fund budget.
- In total, we are requesting \$1,914.4 million in funds for the department.
- The budget proposes increased funding of \$6.0 million for developmental disabilities. Of this amount, \$1.6 million will be used to provide services to 50 additional clients. In total, more than 7,100 developmentally disabled clients will be funded by the state.
- We include a \$3.6 million increase to fund caseload and cost-of-living adjustments for the following aging services programs: Old Age Pension, Aid to the Needy Disabled, and Aid to the Blind Supplemental Security Income Colorado Supplement.
- We are requesting nearly \$200,000 to increase staffing at the Mental Health Institutes. Over the last two years we have steadily been increasing staffing levels by 129 FTE at the Institutes.

Corrections

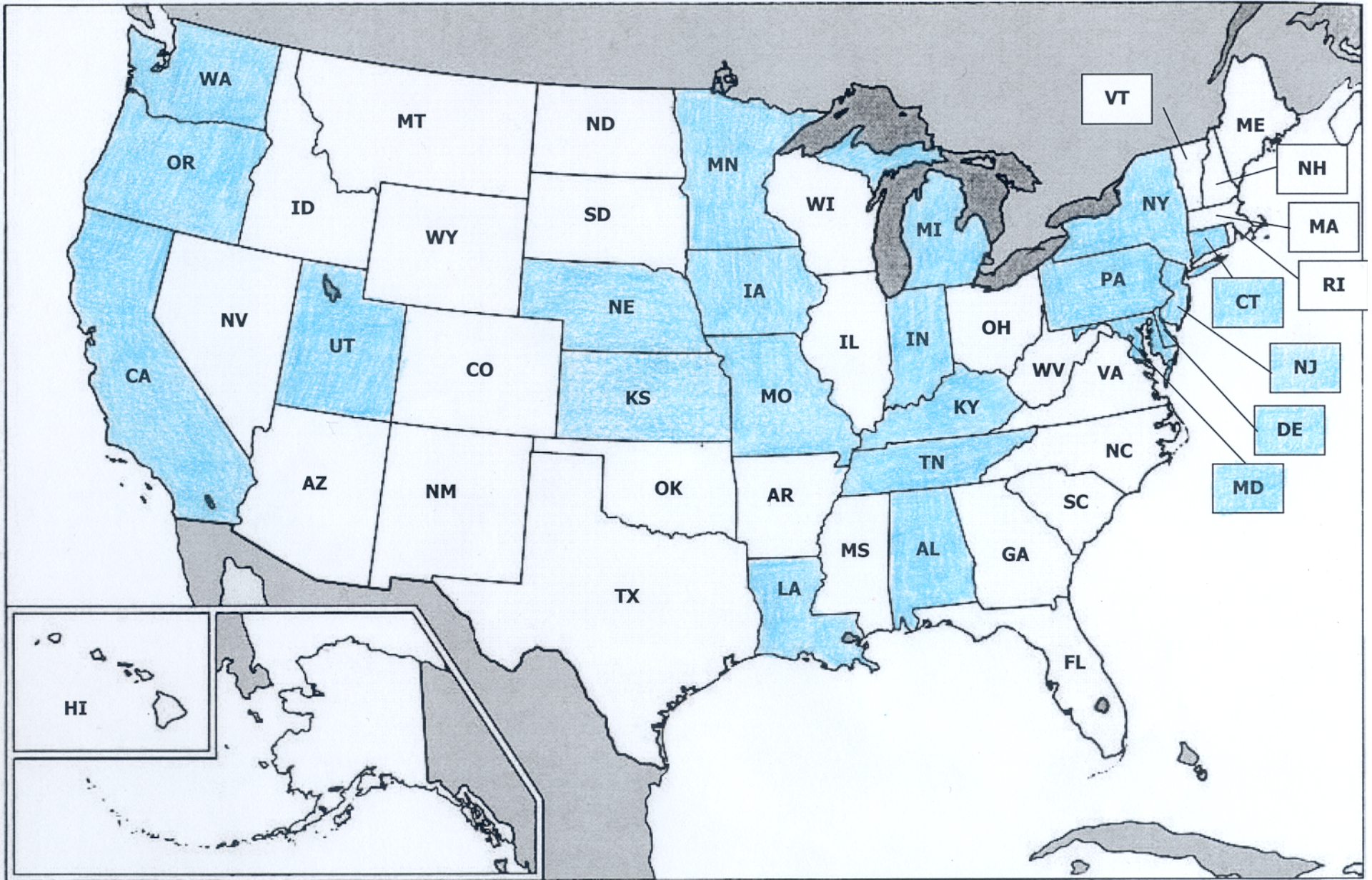
- I am committed to maintaining and improving public safety in Colorado so that all citizens can more safely walk the streets. Toward that end, I am significantly increasing the amount of funds devoted to housing prisoners so that the state can continue to enjoy decreasing crime rates. Due to tough-on-crime policies that include keeping criminals out of our neighborhoods and off the streets, crime in Colorado is at a 22-year low.
- We are requesting a 7.5 percent increase in funding for the Department of Corrections relative to this year's appropriation level. When the current year's four percent budget cuts are taken into account, we are increasing funding in this department by 12.3 percent. These are the strongest growth rates among any of the large General Funded departments.
- We are anticipating that the prison population will increase 8.2 percent in FY 2002-03 and then growth will slow to a 5.4 percent rate in FY 2003-04.

Other High Priority Initiatives

- I am requesting \$4 million for Tony Grampsas grants. These grants are used to divert at-risk youths away from a life of crime. Because of this restoration and the fact that the Department of Public Health and Environment has only a small amount of General Fund, the Department's overall increase is 15.9 percent relative to the original appropriation.
- I am requesting funds for the multi-use network. These funds assure that all areas of the state, including rural and mountainous areas, can access high-speed Internet capability. This will enable the rural areas of the state to provide access to state-of-the-art education programs for their students and to compete in the global marketplace regardless of location.
- Funds for the Veterans Memorial Cemetery in western Colorado. The cemetery officially opened in August 2002.



Graph 1: States with Budget Shortfalls in FY 2001-02



Graph 2: States that Have Increased Taxes and/or Fees

Graph 3: General Fund Revenue Growth

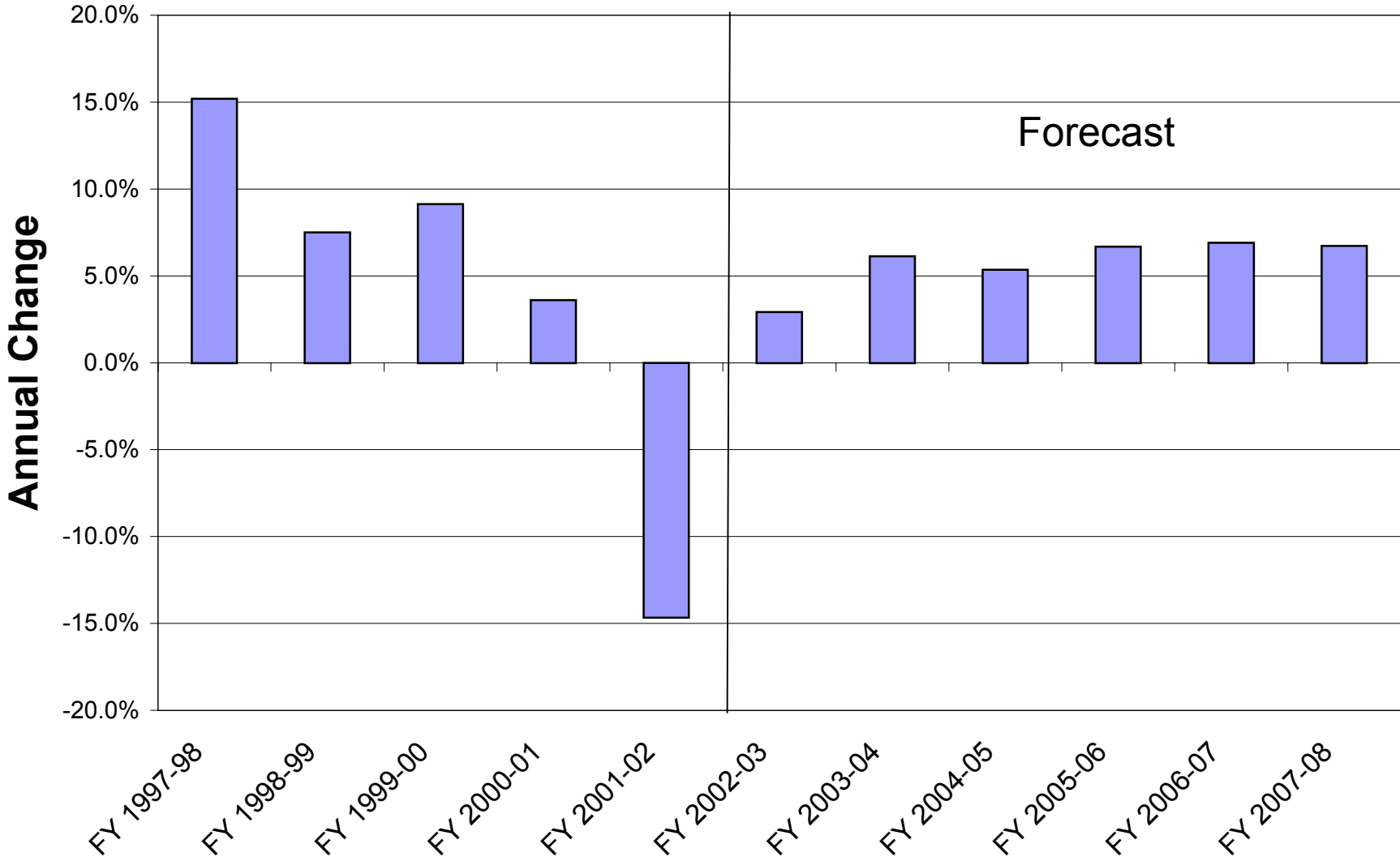


Table 1: Appropriations by Department

	Total FY 2003-04 Request			Percent Change From FY 02-03 Adjusted Appropriation		Percent Change From FY 02-03 Original Appropriation	
	GF	Total - All Funds	FTE	GF	Total - All Funds	GF	Total - All Funds
Executive Departments							
Agriculture	\$ 10,941,729	\$ 31,270,052	298.7	7.3%	1.5%	3.0%	0.1%
Corrections	532,753,788	598,846,500	6,423.8	12.3%	10.8%	7.5%	6.3%
Education	2,493,479,228	3,274,111,185	429.5	3.6%	4.1%	3.6%	4.1%
Governor's Office	19,435,592	40,275,942	124.5	-0.9%	-6.1%	-4.8%	-7.9%
Health Care P&F	1,232,663,474	2,929,960,296	195.6	8.0%	9.3%	4.0%	6.5%
Higher Education	784,162,750	1,641,078,789	155.0	2.4%	3.0%	-1.7%	0.9%
Human Services	537,222,587	1,914,411,287	4,807.6	1.9%	2.4%	-1.9%	0.6%
Labor and Employment	NA	134,459,944	1,096.7	NA	2.1%	NA	2.0%
Local Affairs	9,840,349	185,222,565	182.0	5.3%	2.5%	1.1%	2.3%
Military Affairs	4,934,244	129,113,836	1,159.3	5.5%	0.8%	1.3%	0.6%
Natural Resources	27,693,413	172,522,741	1,551.9	0.9%	-0.8%	-3.2%	-1.5%
Personnel/GSS	15,467,313	153,590,867	594.6	9.2%	3.4%	4.8%	3.0%
Public Health & Envir.	25,049,067	292,061,324	1,120.4	20.7%	3.0%	15.9%	2.6%
Public Safety	60,180,852	204,367,445	1,266.6	5.3%	6.9%	1.1%	5.6%
Regulatory Agencies	2,101,156	73,413,422	540.7	5.9%	-1.6%	1.6%	-1.8%
Revenue	75,606,334	537,893,681	1,522.5	5.1%	0.0%	0.9%	-0.6%
Transportation	NA	39,614,716	227.7	NA	12.7%	NA	12.7%
Total Executive	\$ 5,831,531,876	\$ 12,352,214,592	21,697.1	5.1%	4.8%	2.7%	3.4%
Non-Executive Departments							
Judicial	242,974,565	298,783,657	3,198.3	10.9%	8.6%	6.5%	5.1%
Law	9,273,255	34,458,618	348.5	0.8%	3.6%	-3.2%	2.4%
Legislature (est.)	33,777,911	35,568,234	272.8	6.0%	6.0%	1.8%	2.0%
State	NA	15,859,215	108.6	NA	21.7%	NA	21.7%
Treasury	1,372,295	348,740,067	26.0	5.3%	-1.5%	-1.5%	-1.5%
Total Non-Executive	287,398,026	733,409,791	3,954.2	10.0%	3.5%	5.6%	1.9%
State Total	\$ 6,118,929,902	\$ 13,085,624,383	25,651.3	5.3%	4.8%	2.8%	3.3%

NOTES:

The General Fund column does not include General Fund Exempt.

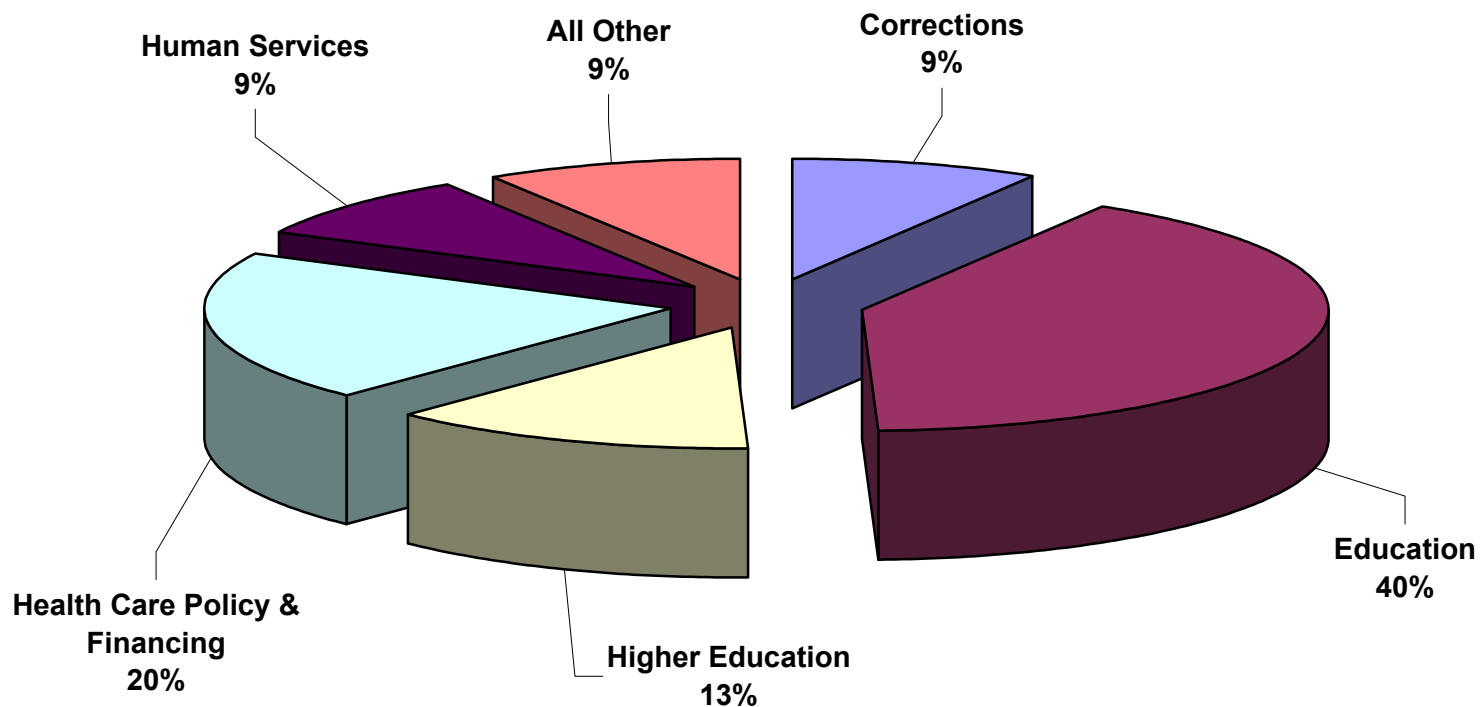
We have assumed a four percent General Fund reduction in Non-Executive departments in order to calculate their FY 2002-03 Adjusted Appropriation

Since we have not received a budget request from the Legislature, we have assumed that they will be requesting six percent growth from their FY 2002-03 Adjusted Appropriation.

Table 2: Expenditure Reductions and Other Actions to Balance the Budget

Budget Changes	2002-03	2003-04	Comments
Lower 6% Expenditures			
Pay Date Change	\$133.89		This will not only save state funds and prevent layoffs, but will also save employees tax payments of roughly \$88 million.
Additional 6% reduction on all departments except K-12, School for Deaf and Blind, Developmental Disabilities, Corrections, and Medicaid. Medicaid takes a 3% reduction, DOC takes no additional cuts.	\$143.20	\$143.20	
K-12, 5% MOE in 02-03 and inflation/enroll MOE in 03-04	\$50.90	\$52.80	Overall K-12 Funding will not change. Only the mix of funds will be changed.
Eliminate Discretionary Free Day Holiday	\$0.50	\$0.50	The savings come because of the overtime the state incurs in 24-hour facilities because of the holiday.
Eliminate GF Fleet Purchases	\$0.29	Already pulled	Cash Funded purchases will be allowed.
Early Retirement Incentives	\$3.63	\$6.68	
Medical Coverage Deduct delayed one month	\$3.96		This results because the state can remit state and employee contributions for health, life, and dental premiums on a different schedule than currently utilized.
Draw federal dollars through local match w/DD	\$2.00		Recent local mill levies passed for the developmental disabilities population may be matched with federal dollars.
Sub-Total 6% Base Reductions	\$338.37	\$203.18	
Non 6% Solutions			
Excess Balance in COPs	\$2.90		This is an excess balance in the COP account.
Cash Fund Transfers:			
ESF Refinance with Reed Act UI Money	\$9.50	\$9.50	
Severance Tax	\$6.64	\$4.56	
DPA Supplier Database CF	\$0.26		
Vital Record Excess Money	\$0.76		
Labor: Major Medical	\$50.00		
Tobacco Trust Fund/ this money will be remitted in the current fiscal year	\$22.70		
Clarify \$30 million Unclaimed Property Transfer	\$30.00		Clarify the state's ability to transfer from the Unclaimed Property Fund into the GF. Because of Accounting standards, the Controller booked a liability to the General Fund for the transfer. Change the law to allow access to this money.
Halve Tobacco Cessation and Research Grants from the Tobacco Fund. Maintain existing funding for all other Tobacco Fund services.	\$11.50	\$11.50	
Tax Amnesty	\$5.00	\$5.00	
Sub-Total Non 6% Solutions	\$139.26	\$30.56	
Grand Total	\$477.63	\$233.74	

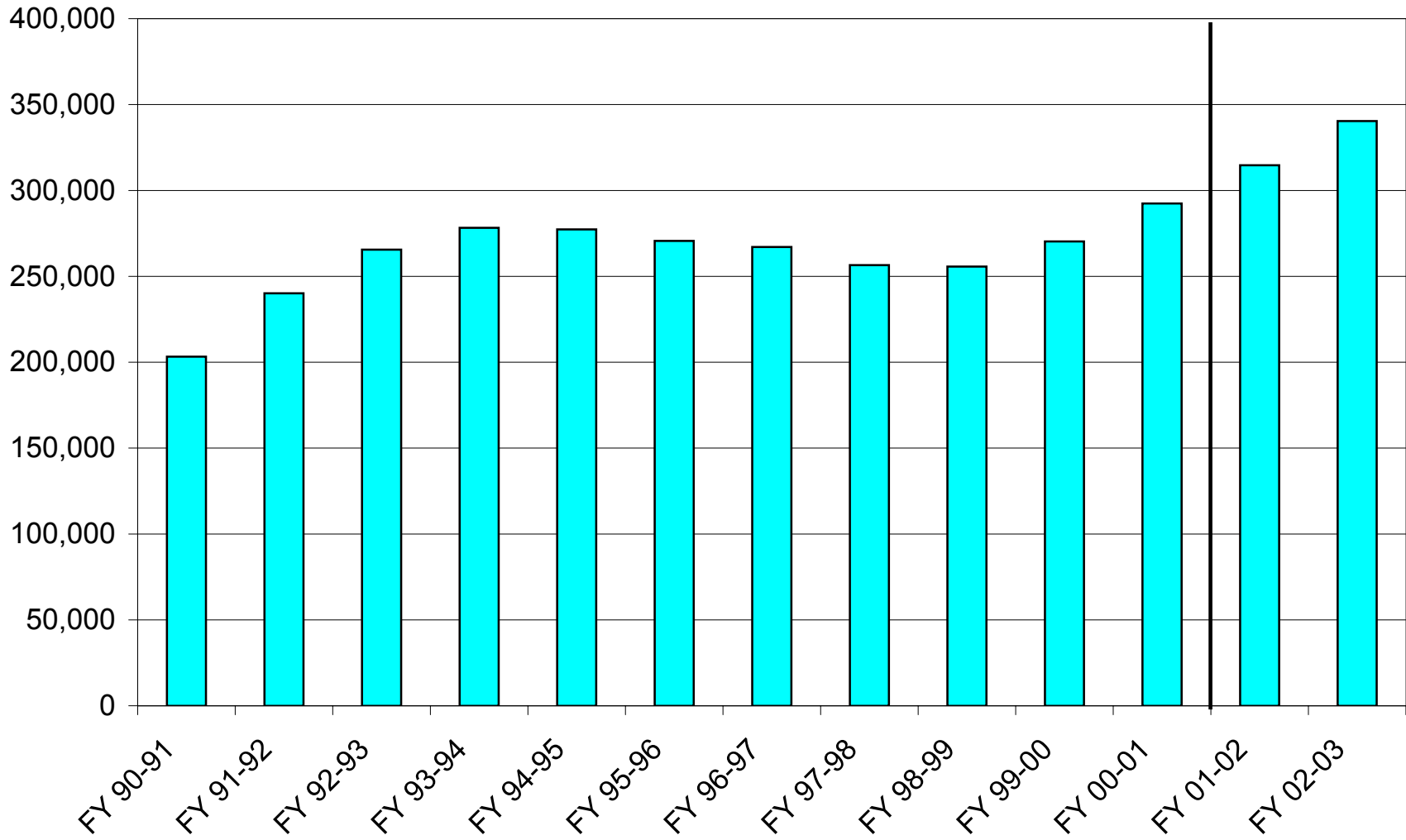
Graph 4: FY 2003-04 Major Department Share of Total General Fund Budget



All Other: Agriculture 0.2%, Governor's Office 0.3%, Labor & Employment 0.0%, Local Affairs 0.2%, Military Affairs 0.1%, Natural Resources 0.5%, Personnel 0.2%, Public Health & Environment 0.3%, Public Safety 1.0%, Regulatory Agencies 0.0%, Revenue 1.2%, Transportation 0.0%, and Non-Executive 4.7%.

Graph 5: Medicaid Caseload

Estimate



STATE OF COLORADO

OFFICE OF STATE PLANNING AND BUDGETING

111 State Capitol Building
Denver, Colorado 80203
(303) 866-3317



MEMORANDUM

Bill Owens
Governor
Dr. Nancy McCallin
Director

TO: Nancy McCallin
FROM: Julie Hart
DATE: September 27, 2002
SUBJECT: General Fund Deficit without Permanent Tax Reductions

The purpose of this memorandum is to analyze the effect of the permanent tax reductions passed in 1999, 2000, and 2001 on the current budget situation the state is facing. With or without permanent tax reductions, the state still would have had a deficit in FY 2001-02. In fact, if taxes had not been reduced, the General Fund budget deficit would have been worse in FY 2001-02. This is because the General Assembly typically spends the TABOR surplus when it comes in the door, then waits until the following year to pay the TABOR refund. Without permanent tax cuts, the TABOR surplus would have been higher and the General Assembly would have spent some or all of it. Then, in the following year, the refund would be much higher. On average, the General Assembly spent almost the entire TABOR surplus. As a conservative estimate, if we assume the General Assembly spent \$200 million more per year in fiscal years 1999-00 and 2000-01 on capital expenditures and there were no permanent tax cuts, the General Fund deficit would have been \$1,457.6 million in FY 2001-02. Instead, with the tax cuts, the deficit totaled \$1,389.4 million. Therefore, the deficit with permanent tax cuts was \$68.2 million less than what would have occurred with no permanent tax cuts. Moreover, a more likely scenario occurs assuming the General Assembly spent all the excess General Fund reserve on capital. If this occurred, the deficit would have reached \$1,879.6 million in FY 2001-02.

Why Do the Permanent Tax Cuts Help the Budget?

The budget deficit in FY 2001-02 was less than what would have occurred if there were no permanent tax reductions. This occurs because of the TABOR refund. The state is constitutionally required to return all TABOR revenue that exceeds the TABOR limit each year. Therefore, since the state was in a TABOR surplus position in 1999, the Governor and the General Assembly decided to let the citizens of Colorado keep their money rather than turning it into the state to have it refunded the following year. Without the tax cuts the state would have had a bigger TABOR refund liability (\$1,529 million compared with \$927 million) in FY 2001-02 and thus a larger deficit.

In addition, it is important to note that the tax cuts have helped the economy in the past few years. The permanent tax reductions put \$480 million in the pockets of Colorado's citizens each year. Thus Coloradoans have a higher after-tax income and are able to spend more. In addition, the opportunity cost to taxpayers of the state holding the TABOR money for one year before refunding it is approximately \$27.5 million per year.