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TOP STORY

Budget writers will have to cut $3.3 billion from general fund, new numbers show

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The largest revenue shortfall in state history will translate into a $3.3 billion cut to the state budget for 2020-21, according to an updated revenue forecast presented to the Joint Budget Committee on Tuesday morning.

General fund revenues — made up of individual and corporate income taxes, and sales and use taxes — are estimated to be down more than $2 billion in 2020-21.

A precipitous drop in oil and gas activity compounds the problem, according to Kate Watkins, chief economist for the Legislative Council.

While the state budget for 2020-21 as proposed by Gov. Jared Polis was expected to be around $34.5 billion, the $3.3 billion shortfall is entirely general fund. That's about one-third of the state budget, and that shortfall translates into a 25.3% drop compared to 2019-20 spending, Watkins said.

That may not be the end of it, she added. Inflation and caseload pressures could drive that shortfall higher.

The $3.3 billion shortfall is a combination of where the state ends with the 2019-20 budget, with a shortfall of $895.8 million and declines in general fund of $2.42 billion. That's actually not as bad as it could have been, given that Polis ordered cuts to the 2019-20 budget on March 30.

A forecast from the governor's Office of State Planning and Budgeting estimated the shortfall at $2.7 billion less than the 2019-20 budget.

Decline in commercial real estate, also impacted by oil and gas activity, will soften the non-residential share of real estate property taxes. That could have an impact on school finance, given that property taxes make up 40% of the funding for K-12 schools. However, residential real estate prices and demand should hold steady, Watkins said.

The biggest drop in revenues is from individual income tax, according to the legislative council forecast, down 60.7%. Sales and use taxes are expected to be down some 27.1%.

Economist Greg Sobetski of the Legislative Council pointed out that businesses that incur losses don't owe income taxes and don't make estimated tax payments. That's leading to more volatility in income tax collections than in the overall economy, he said.

For regional activity, Watkins said Weld County will be especially hard hit by the drop in oil and gas production and revenues.

Among risks to the forecast, Watkins said the economic recovery could take longer, and that could result in more layoffs and business declines. She also said it's possible the state could experience a deep recession.

Just how fast, or slow, the economic recovery would take is largely based on whether COVID-19 can be contained and treated, she said.

The Coronavirus Aid, Relief and Economic Security Act, the $2.2 trillion aid package passed by Congress on March 26, isn't helping, according to the legislative council presentation. Economists predict the bill will actually decrease state revenues from corporate and income taxes. That's because it provides additional deductions for businesses and delays taxable income for retirees.

The CARES Act impact to general fund revenue is $121 million less in 2019-20 and $135 million less in 2020-21, the forecast said. The OSPB forecast showed a larger impact, with $86 million less for 2019-20 but $272 million less for 2020-21.

The CARES Act does have one upside, according to Sobetski. The money that went to businesses and individuals have somewhat stemmed the decrease in total economic activity, meaning that expectations for income and sales tax are "less bad" than they would have been.

Sobetski explained that the act changed tax policy, which changes how much taxpayers pay in Colorado. CARES reversed deductions tied to the 2017 Tax Cuts and Jobs Act, Sobetski said, most notably ending a limit on excess business losses.

State economists also took a deep look at oil and gas activity, which is also affecting the forecast. The price of crude oil was down to $15.71 per barrel on May 1, down from $45.60 per barrel just two months earlier.

Stay-at-home orders have caused a 36.9% decline in oil consumption, and that's meant more than $100 million less in severance taxes. That's the tax that producers pay to "sever" the minerals from the ground, and which has been a steady source of income for the state to fund water projects, for example. Legislative Council Economist Meredith Moon said the "break-even" point for producers in the Denver-Julesburg Basin is about $50 per barrel, and expects demand to be lower for years to come.

That means severance tax collections will be depressed for the next three years. The lower oil and gas activity impacts corporate income taxes, too, she said, and 12% of "direct industry workers" have been laid off, she said.

There's another place where economists looked, at that's at the state's unemployment insurance trust fund. According to the presentation, the trust fund is expected to be insolvent, short $2 billion in 2020-21 and $2.5 billion the following year.

The shortfall is a combination of lower (or none at all) unemployment insurance payments coming in from shuttered businesses and a dramatic increase in unemployment claims. Legislative Council Economist Elizabeth Ramey told lawmakers that the unemployment trust fund has been insolvent before, during the Great Recession.

As of April 2020, weekly average unemployment claims were 56,800, compared to 1,900 per week a year ago. The total number of Coloradans filing for unemployment, according to Luke Teater of OSPB, is more than 400,000.

The OSPB forecast showed that unemployment is higher in mountain communities, an average of 21.6%. Only the Eastern Plains has unemployment below double-digits, at 9.2%. But the OSPB forecast also said that unemployment has been hardest on industries with low wage earners.

OSPB also took at look at tourism spending, showing that between the first of February and end of April, spending is down more than 80%.

JoAnn Groff, the state's property tax administrator, also gave grim news to the JBC about the impact of property taxes in 2020-21. She said she expects a 36% drop in oil and gas property taxes, an almost equally large reduction in commercial property taxes, and a lower assessment rate for residential, based on the constitutional requirement that requires a 55/45 split between commercial and residential property taxes. School districts that rely o property tax -- and there are some that are fully funded by property taxes -- will see a negative impact to their revenues based on the COVID-19 impacts to property taxes, both from the residential property tax rates and from lower values of commercial and oil and gas properties, she said.

About a half-dozen lawmakers, including Speaker of the House KC Becker, a Boulder Democrat, also sat in on the presentation.

Senate and House Democrats on the JBC pledged to do as much as possible to protect schools and protect public health and safety services.

“Colorado is facing what may be the most dire budget situation in our state’s history, but I know that we will join together and meet this challenge," said JBC Chair Rep. Daneya Esgar, a Pueblo Democrat.

"The JBC has been working hard to protect vulnerable Coloradans and soften the impact of these cuts, as we prioritize education and critical health and safety services," Esgar said. "We’re exploring every possible option for how we can best support our state’s recovery, but it’s critically important that Congress provide additional aid if we are to minimize the impact of these cuts on our schools and essential services.”

“This forecast confirms what we have anticipated for some time: there will certainly be painful decisions ahead,” said Sen. Rachel Zenzinger, an Arvada Democrat. “We must figure out how to do more with much less. Nevertheless, we remain steadfast in our convictions to ensure anticipated cuts do not fall disproportionately on our students, schools or health and safety programs.”

For now, that means the state cost for paying for full-day kindergarten, at $220 million, is still in the 2020-21 budget, as is $60 million for the second year of the state's reinsurance program, at a cost of $60 million. Polis is committed to keeping those costs in the budget.

Polis spokesman Conor Cahill told Colorado Politics Monday “the Governor is committed to ensuring every child has access to a full day of free kindergarten and saving people money on healthcare. Now is certainly not the time for Coloradans to have to worry about more money coming out of their already thin pocketbook for education and health care.”

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