

Bill Levine Talks State Funding for Water Programs



Southwestern Water Conservation District – Annual Seminar

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presentation, please contact:

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Colorado's Water Plan

- Colorado's population could nearly double by the year 2050.
- This population growth will increase the demand for water. Colorado's could experience a water supply gap of up to 560,000 acre feet by the year 2050.

Colorado's Water Plan

- Through a mix of water conservation, additional water storage, improved land use planning, alternative transfer methods, and reuse, Colorado's Water Plan sets a measurable objective of reducing the municipal and industrial water gap to zero by the year 2030.

Colorado's Water Plan

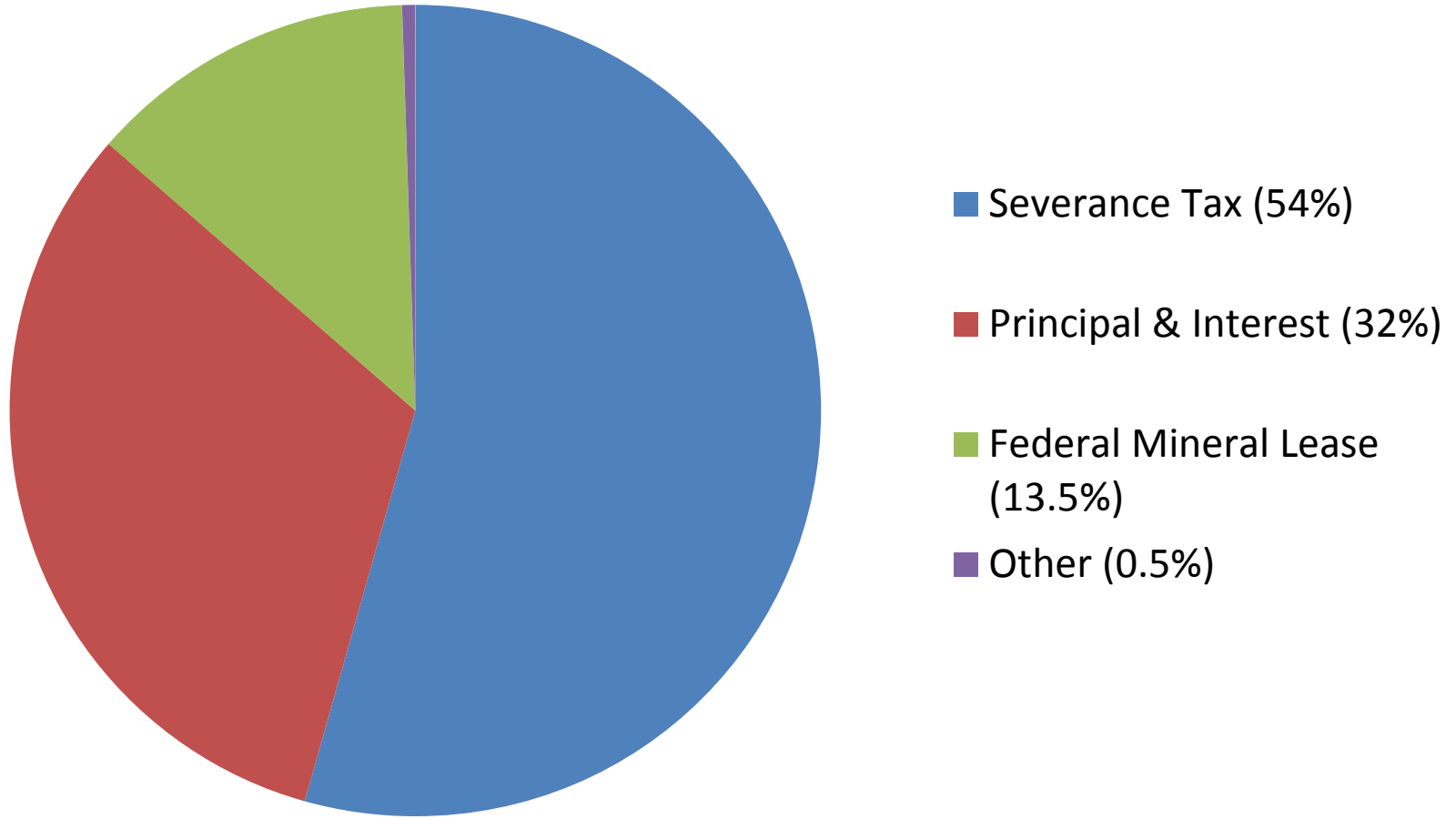
- Colorado's Water Plan sets an objective to sustainably fund its implementation. In order to support this objective, the State will investigate options to raise additional revenue in the amount of \$100 million annual starting in the year 2020 (providing a total of \$3 billion in additional state funding by the year 2050).

State Funding for the Colorado Water Conservation Board (CWCB)

Some of the CWCB's Major Programs:

- Grants and Loans for Water Projects
- Water Supply Planning
- Watershed Protection & Floodplain Mapping
- Instream Flow Program
- Interstate Compacts
- Endangered Species Protection
- Water Efficiency Program & Drought Planning

A Look at CWCB's Total Revenue Streams



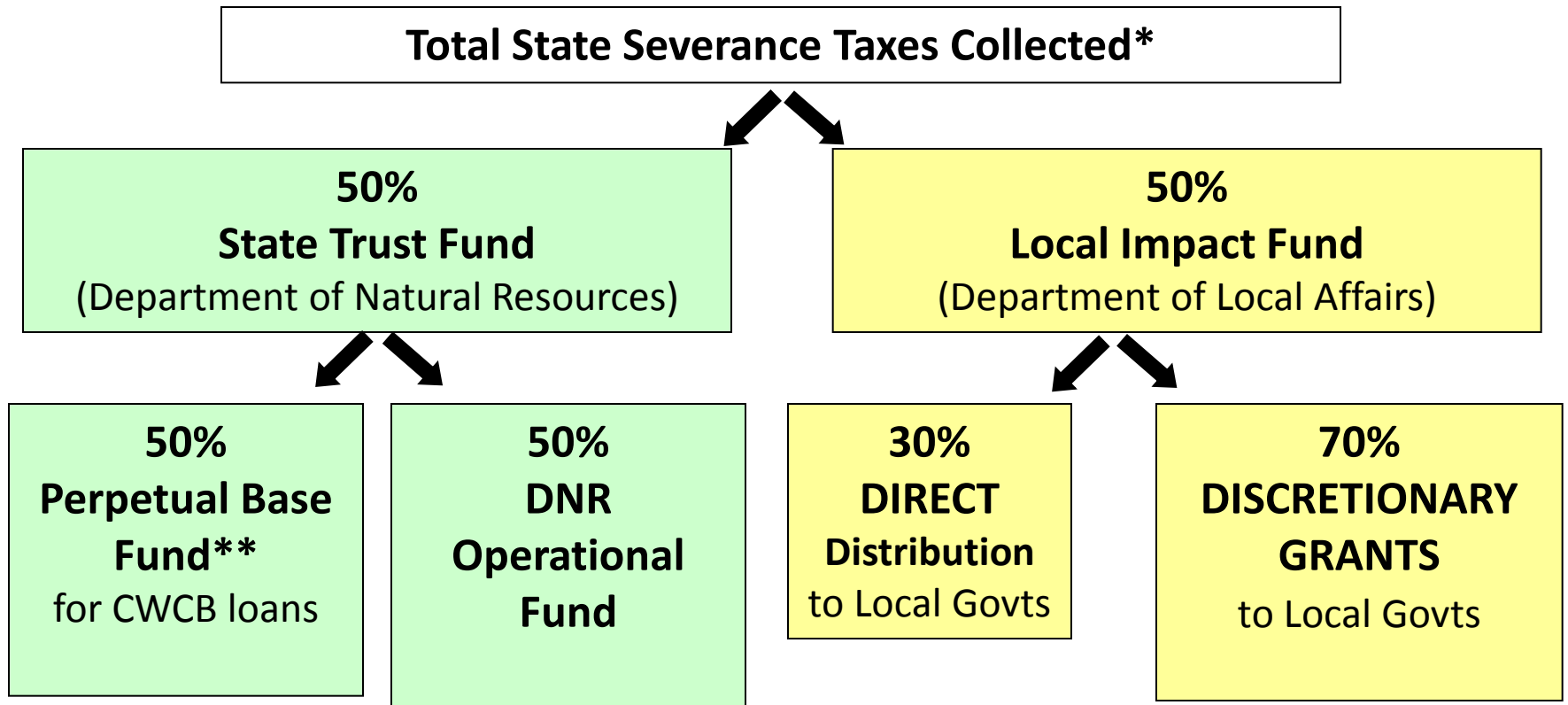
Federal Mineral Lease (FML) Revenue

- The State of Colorado receives 50 percent of the net sales, bonuses, royalties, and rentals of federal lands in Colorado. This generates about \$150 million per year (although revenue rises and falls with commodity prices).
- Of this amount, ten percent of the non-bonus payment revenue flows to the CWCB. CWCB got \$14.4 million in FY 2014-15 and \$8.6 million in FY 2015-16 from this revenue source. CWCB has received an average of \$13.5 million in FML over the last 8 years.
- FML also supports K-12 Education, Higher Education, and Local Governments.

What is Severance Tax?

- Severance Tax is a tax on nonrenewable minerals as they are “severed” from the earth.
- There are separate severance taxes on oil and gas, coal, metals, and oil shale
- Severance tax revenue from Oil and Gas development has generated 95% of the severance tax revenue over the last five years.

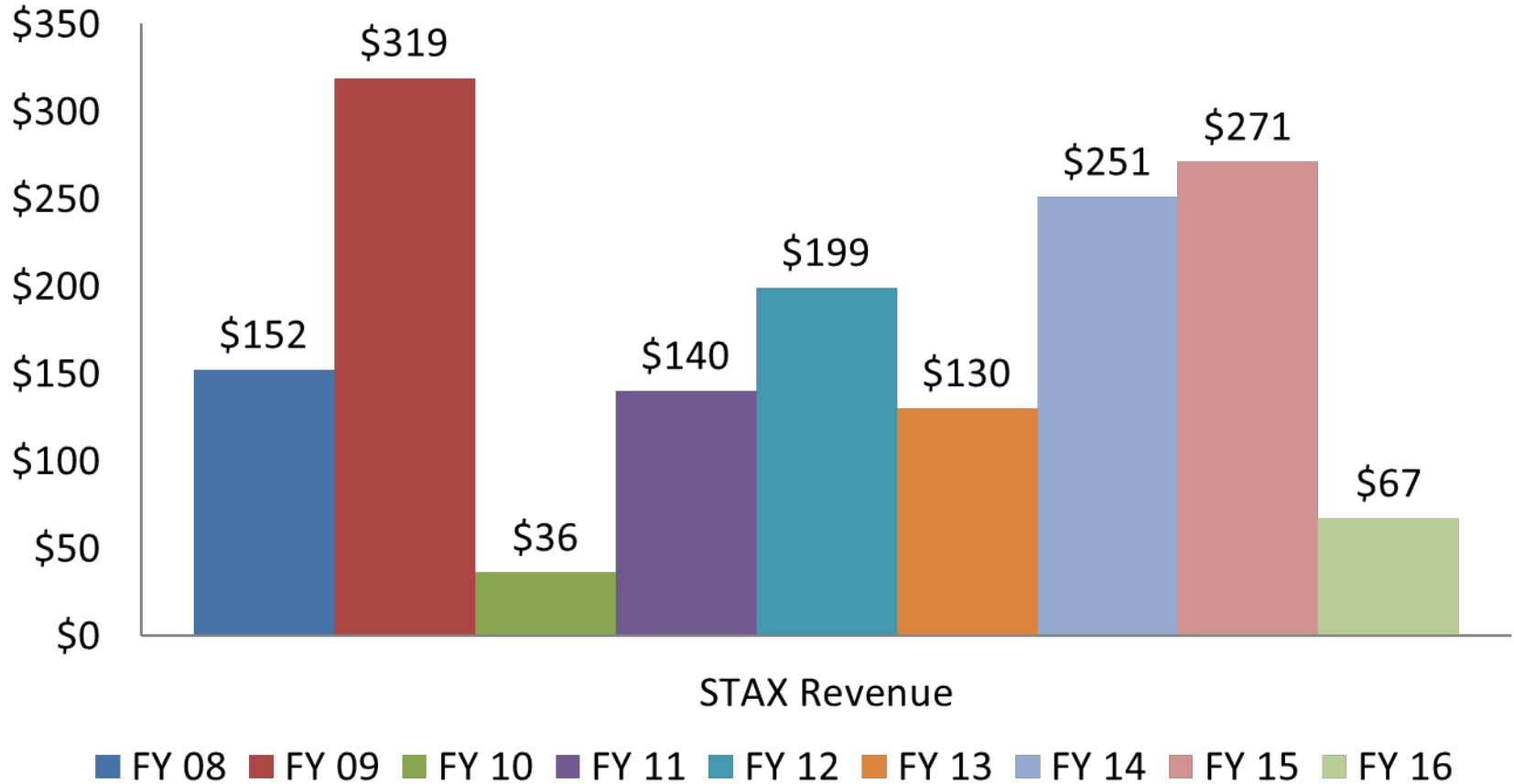
How is Severance Tax Distributed?



* \$1.5 Million of severance tax is taken “off-the-top” and deposited into the Innovative Energy Fund

** If Perpetual Base Account revenues exceed \$50M; next \$10M flows to CDPHE’s Small Communities Water and Wastewater Grant Fund.

History of State's Severance Tax Revenue



WTF?



Why

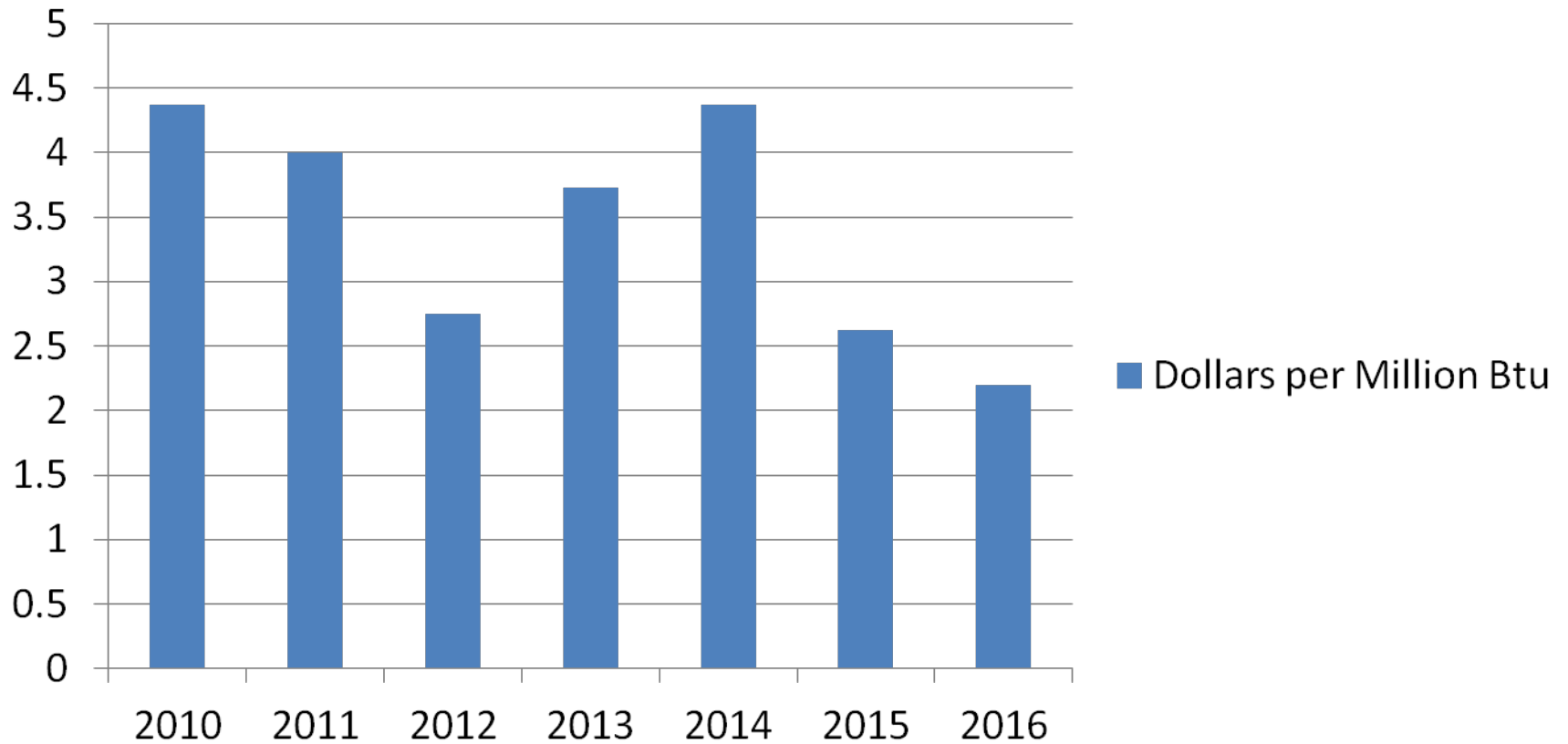
The

Fickleness?

(WTF)

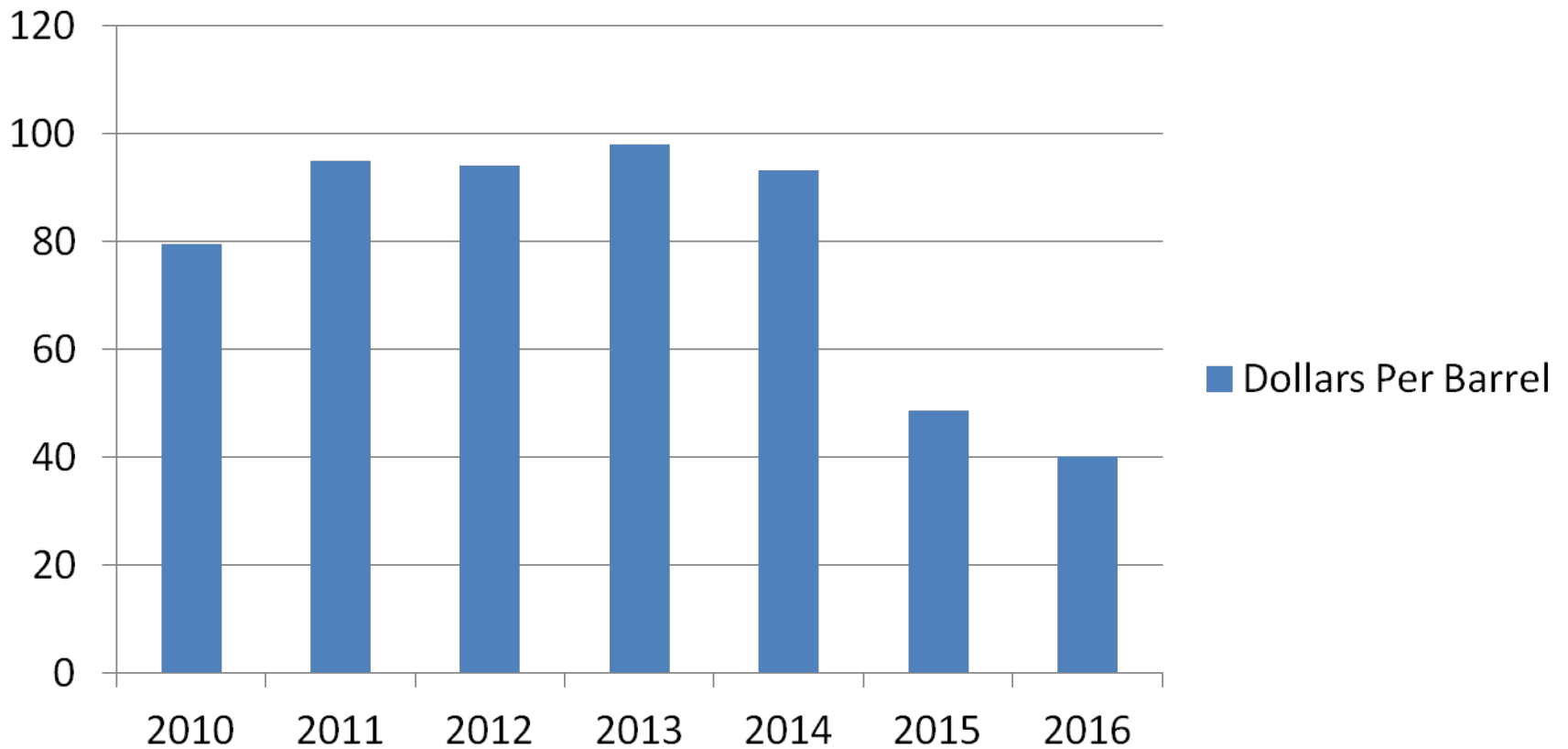
Henry Hub Spot Natural Gas Prices

Spot Prices at Henry Hub



Spot Prices for Crude Oil

WTI Crude Oil Prices



So if Energy Prices Got Cut in Half, Why Did Severance Tax Revenue Go Down by 75%?



Impact of the Ad Valorem Offset

- Colorado law provides a credit equal to 87.5% of the ad valorem taxes that may be applied to oil & gas related severance tax liabilities.
- The ad valorem offset is reflective of conditions two years ago. In this regard, the ad valorem offset increases revenue volatility.

Not Just Volatile, But Unpredictable

Recent Revenue Forecasts by LCS

	FY 10	FY 11	FY 12	FY 13	FY 14	FY 15	FY 16	AVG
Dec Forecast	\$85	\$177	\$171	\$122	\$182	\$312	\$75	\$161
Actual Revenue	\$48	\$149	\$208	\$139	\$269	\$280	\$71	\$166
Variance (\$)	(\$37)	(\$27)	\$37	\$16	\$86	(\$31)	(\$4)	\$26*
Variance (%)	(44%)	(15%)	22%	13%	47%	(10%)	(5%)	18%*

BP America v. CO Dept. of Revenue



Supreme Court Ruling on the BP Case

- The Colorado Dept. of Revenue has historically not allowed producers to claim a return on investment (ROI) as a valid deduction against severance tax liability
- ROI is defined as the opportunity cost of a capital investment that an investor could have earned on a similar investment of similar risk.
- Opportunity cost is not an expense that is actually paid by the investor.

Supreme Court Ruling on the BP Case

- The Colorado Supreme Court ruled that state statute clearly allows the deduction of “any transportation, manufacturing, and processing cost”, including ROI.
- The Supreme Court ruling did not establish how exactly ROI should be calculated.
- ROI was the primary focus of the Supreme Court case but may have implications on other Netback Expense Report Form (NERF) deductions. NERF Deductions, including ROI, are allowed by the Property Tax Administrator.

S.B. 16-218

- To help pay for refunds related to the *BP v. Colorado Department of Revenue* case, the General Assembly passed S.B. 16-218. This legislation provided that the majority of severance tax refunds be paid out of the General Fund.
- S.B. 16-218 restricted moneys in each of the 3 cash severance tax cash funds in case funding was needed to assist in paying these refunds.
- Through February 2017, the General Fund has already provided over \$113 million of support towards paying severance tax refunds pursuant to S.B. 16-218.

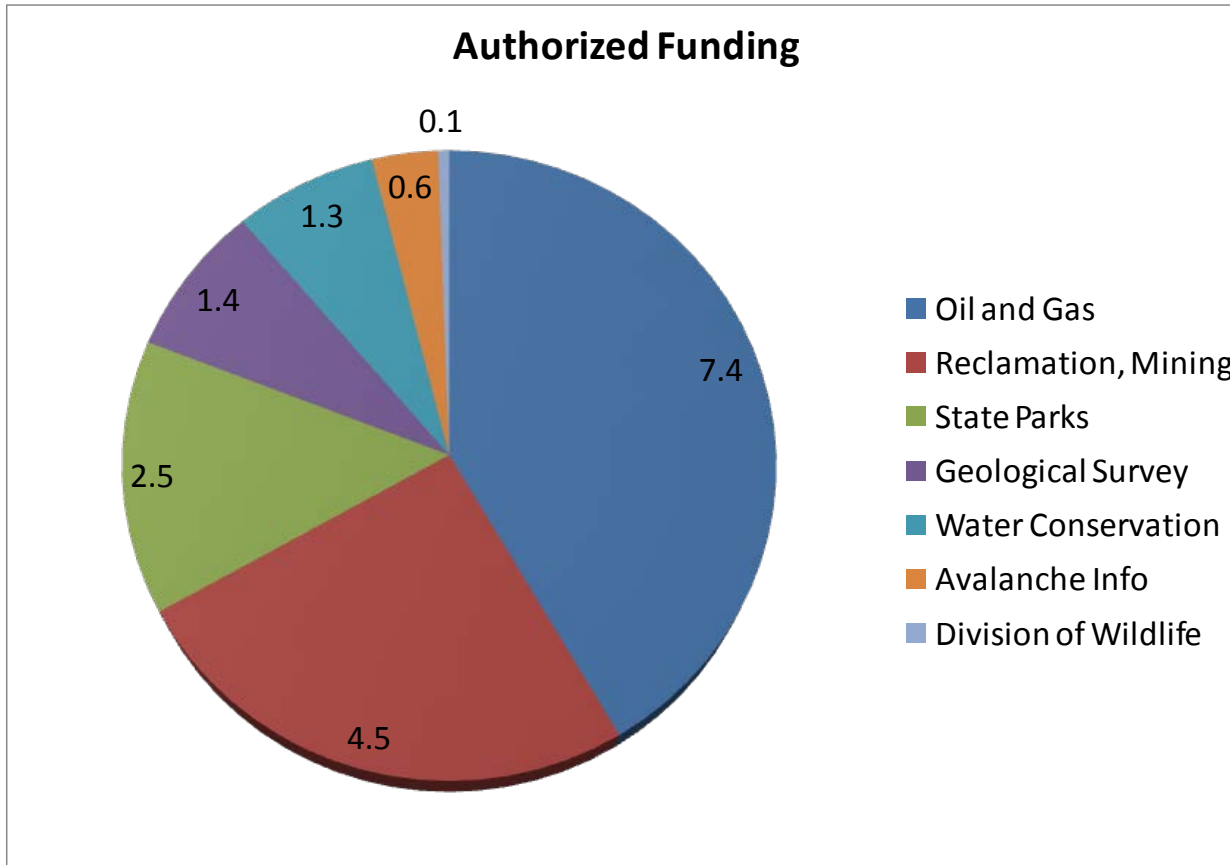
Executive Branch's FY 2017-18 Budget Request

- The Governor's FY 2017-18 Budget Request proposes to transfer \$31.7 million of the \$57.5 million in severance tax funds still restricted under S.B. 16-218 to the State's General Fund.
- In addition, on January 3rd of 2017, the Governor proposed transferring another \$45.7 million of severance taxes to help balance the State's General Fund budget.
- To balance the State's FY 2017-18 General Fund budget, the General Assembly will only transfer the \$45.7 million (but not the additional \$31.7 million) in severance tax revenue to the General Fund.

Perpetual Base Fund Outlook

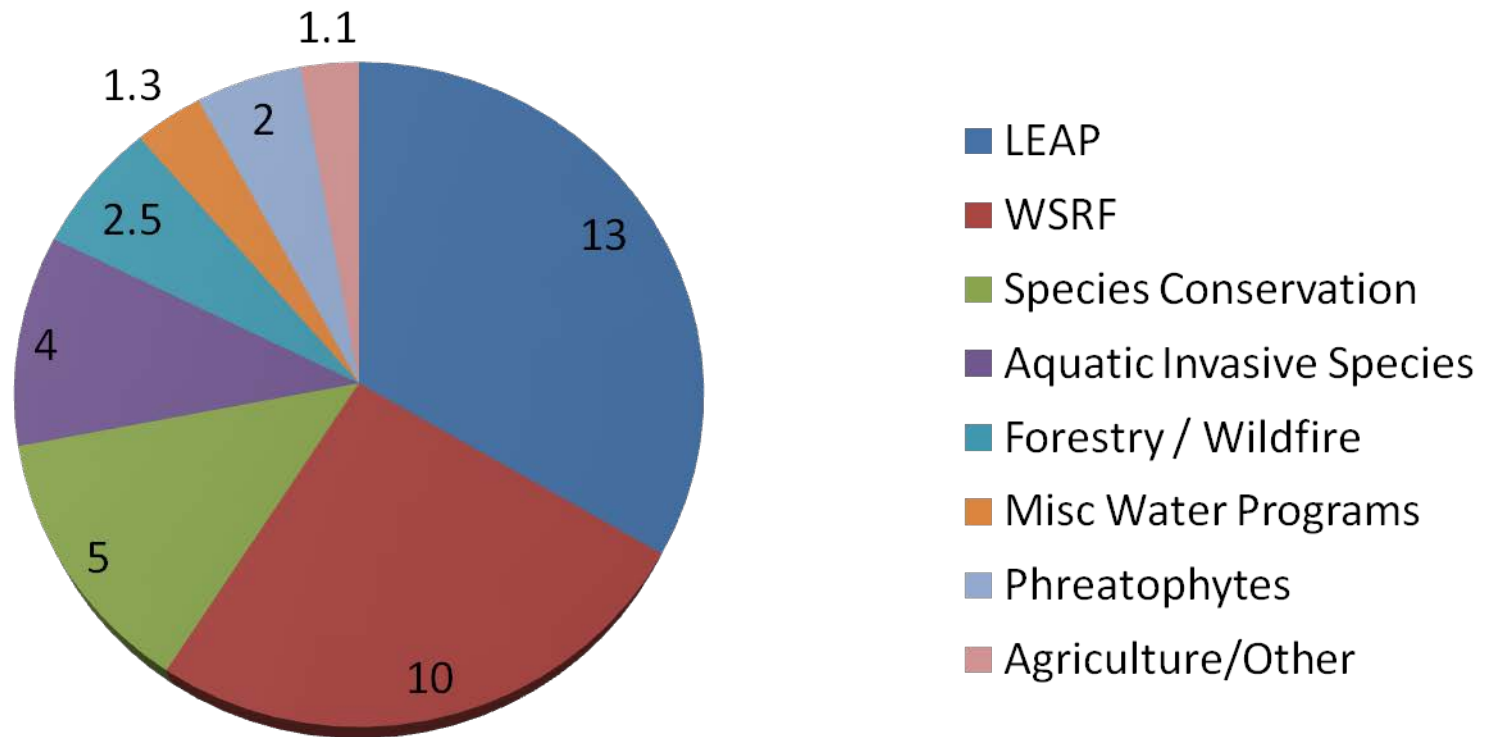
- The Perpetual Base Fund is a revolving loan fund used primarily for water project loans.
- For FY 2016-17, the Fund will earn an estimated \$23 million in revenue, including almost \$18 million in new severance tax revenue as well as principal and interest repayments on water loans.
- In FY 2017-18, the Fund will earn an estimated \$30 million in revenue, including almost \$25 million in new severance tax revenue as well as principal and interest repayments on water loans.

Operational Fund -Tier 1 program authorizations in FY 2016-17



Operational Fund -Tier 2 program authorizations in FY 2016-17

Authorized Funding



Putting it All Together FY 17

- Tier 1 appropriations for FY 2016-17 total \$18 million
- Tier 2 authorizations for FY 2016-17 total \$39 million
- This total spending (\$57 million) will be supported by an estimated \$18 million in Severance Tax Operational Fund revenue projected for FY 2016-17.
- Tier 1 programs will be fully funded, but the requirement to hold 100% of Tier 1 spending in reserve will be missed by \$9 million if moneys held in restriction by S.B. 16-218 are not released.
- Tier 2 programs will receive no funding in FY 2016-17.

Putting it All Together FY 18

- Tier 1 appropriations for FY 2017-18 total \$16 million
- Tier 2 authorizations for FY 2017-18 total \$34 million.
- Total spending (\$50 million) will be supported by an estimated \$24 million in net revenue projected for FY 2017-18. Additionally, the General Assembly might release the \$10 million restriction per S.B. 16-218.
- After funding Tier 1 expenses, about \$9 million will be needed for the Tier 1 reserve.
- Tier 2 programs will receive no funding in FY 2017-18 if the \$10 million remains restricted. However, if the entire \$10 million were released, Tier 2 programs would each get about 30% of authorized funding.

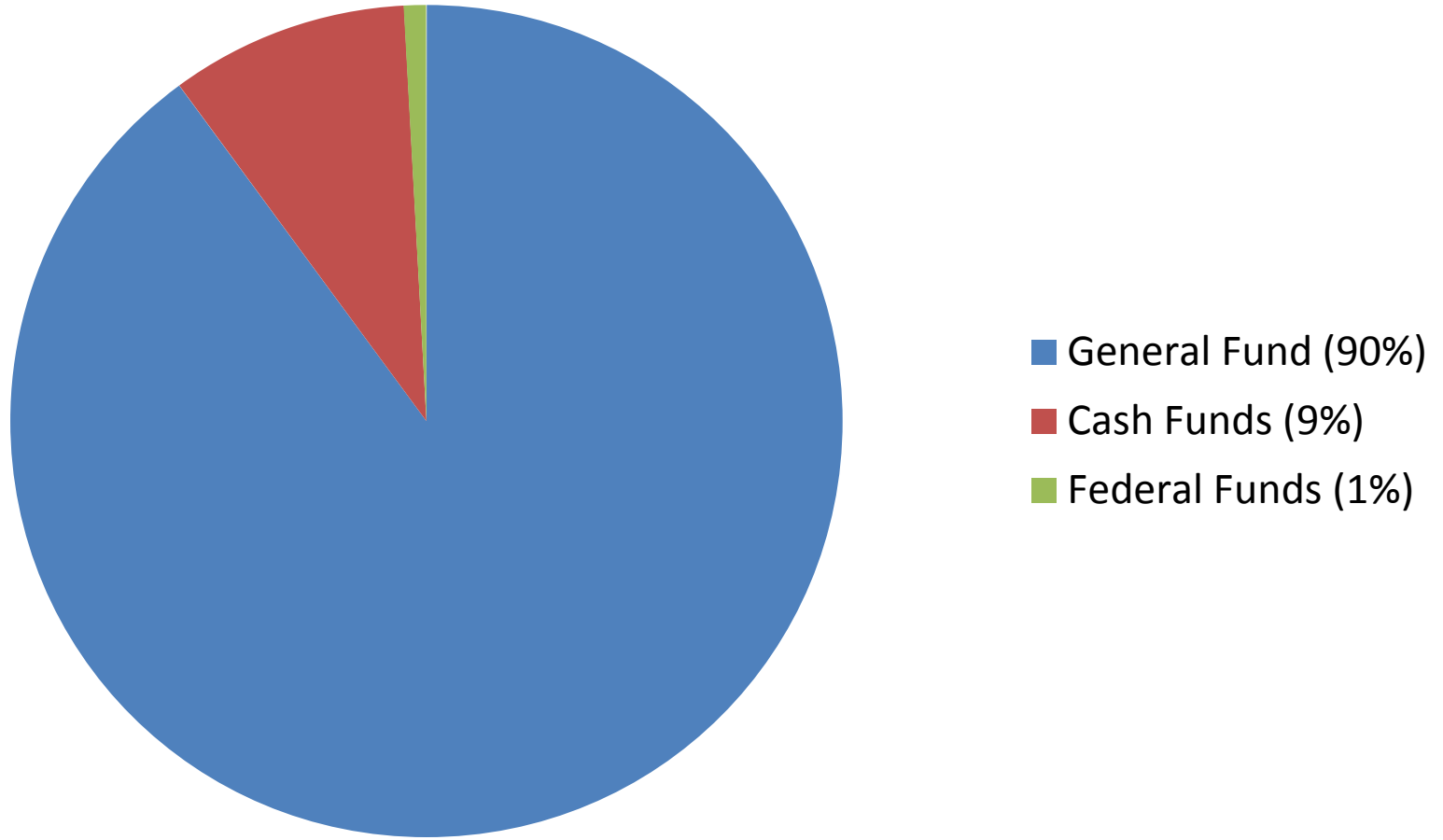
Longer Term View: Why the Severance Tax Operational Fund is Over-Allocated

Average Future Year	Estimated Spending
Average Yearly Severance Tax Revenue	\$174.0 million
<u>25% of Average Yearly Severance Tax</u>	<u>\$43.5 million</u>
Tier 1 Spending Authorizations	\$15.7 million
Tier 2 Spending Authorizations	\$36.9 million
Total Spending (Tier 1 + Tier 2)	\$52.6 million
Amount Out of Balance	(\$9.1 million)
Estimated Funding for Tier 2 Programs	75%

Division of Water Resources

- The Division of Water Resources (DWR) consists of two major programs: administration of water rights in Colorado (including both intrastate water rights and interstate compact enforcement) as well as operation of the Dam Safety Program.

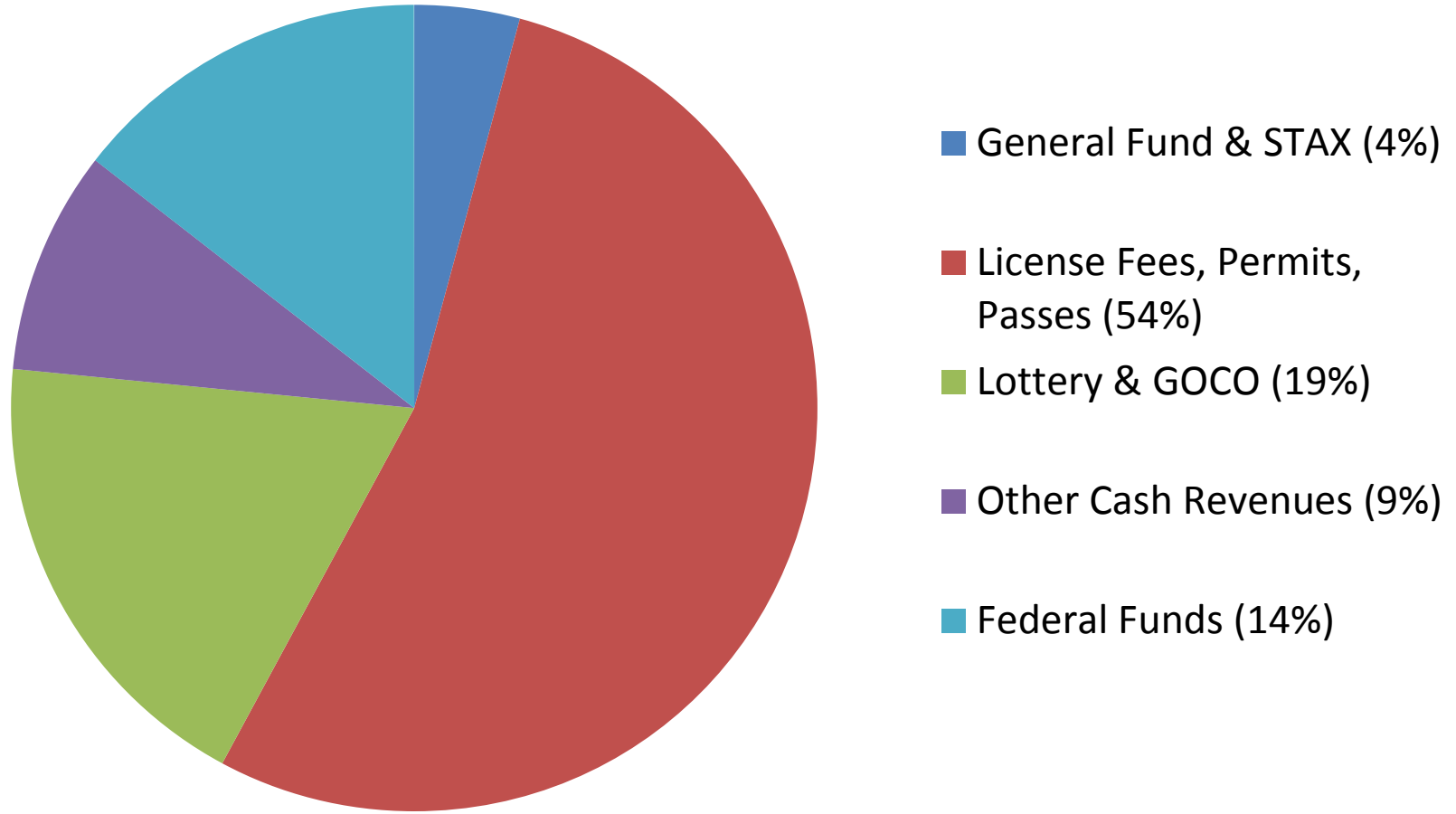
A Look at DWR's Budget



Colorado Parks and Wildlife

- Operates 42 State Parks
- Manages the Trails Program and Outdoor Recreation both in and out of state parks
- Manages hunting and fishing programs
- Manages about 350 state wildlife areas
- Manages the State's wildlife, including the protection of threatened and endangered species
- Monitors over 200 waters in Colorado for aquatic invasive species and inspects of 400,000 watercraft in an attempt to prevent the spread of aquatic nuisance species.

A Look at Colorado Parks and Wildlife's Revenues in FY 2015-16



Understanding the Greater Budget World We Live In



Taxpayer Bill of Rights (TABOR)

- TABOR is a revenue limiting amendment to the State Constitution that was adopted in 1992.
- Under TABOR, state and local governments may not raise tax rates without voter approval
- TABOR creates a cap of the amount of revenue state and local governments may collect. Each year, the cap grows by inflation plus population growth.

TABOR Continued

- If revenue is collected above the TABOR revenue cap, it must be refunded to taxpayers (unless voters approve retaining excess revenues).
- At the State level, TABOR refunds are paid out of the General Fund.
- Not all revenue is subject to TABOR. Federal funds, for example, are TABOR exempt.
- Revenue collected from an “enterprise” is also exempt. Enterprises are created by statute, have bonding authority, and collect less than 10% of their revenue from the State.

TABOR Continued

- In its March 2017 Colorado Outlook, the Governor's Office projected that the State would be about \$135 million over the TABOR cap in FY 2017-18 and \$145 million over the cap in FY 2018-19. The \$145 million translates to \$41 per Colorado taxpayer.

The General Fund

- The State General Fund receives about \$10.5 billion per year in revenue.
- Source of revenue include sales taxes (roughly \$3 billion), individual and corporate income taxes (roughly \$7.2 billion), and other sources of income (roughly \$0.3 billion).
- The General Fund is the State's general purpose fund and finances a wide variety of programs and projects.

Colorado's General Fund Budget

Item	Amount	% of Total
K-12 Education	\$3.48 B	36.7%
Health Care Policy and Finance (Medicaid)	\$2.50 B	26.3%
Higher Education	\$0.86 B	9.1%
Human Services	\$0.82 B	8.6%
Corrections	\$0.76 B	8.0%
16 Other State Departments	\$1.04 B	11.0%
<u>Department of Natural Resources</u>	<u>\$28 Million</u>	<u>0.3%</u>
Total FY 2015-16 Operating Appropriations	\$9.49 B	

FY 2017-18 General Fund Budget Outlook (from Late 2016)

Item	Amount	Source of Requirement
K-12 Education – New Enrollment and Inflation	\$243.5 M	State Constitution
TABOR Refund	\$195.0 M	State Constitution
Refill Budget Reserve from FY 2016-17	\$190.8 M	State Statute / Policy
H.B. 09-228 Transportation and Capital	\$164.0 M	State Statute
<u>New Medicaid Costs</u>	<u>\$142.8 M</u>	<u>Federal & State Statute</u>
Total New Spending	\$926.1 M	
<u>Total Available New General Fund Revenue</u>	<u>\$426.0 M</u>	
Minimum Funding Gap	\$500.1 M	

Putting It All Together: Balancing the General Fund Budget

- To eliminate projected TABOR refunds paid out of the General Fund, the General Assembly has capped the amount of hospital provider fee revenue the State may collect for the State's Medicaid program. This equates to a \$264 million cut. Since this money is used to match federal Medicaid dollars, the State's Medicaid program loses a total of \$528 million.

Putting It All Together: Balancing the General Fund Budget

- The General Assembly now includes a “Negative Factor” to the School Finance Act.
- Critics charge that this is a workaround the Amendment 23 requirement that K-12 funding grow each year by inflation plus student enrollment growth. These critics believe that the negative factor may be responsible for K-12 education being about \$1 billion lower than required.

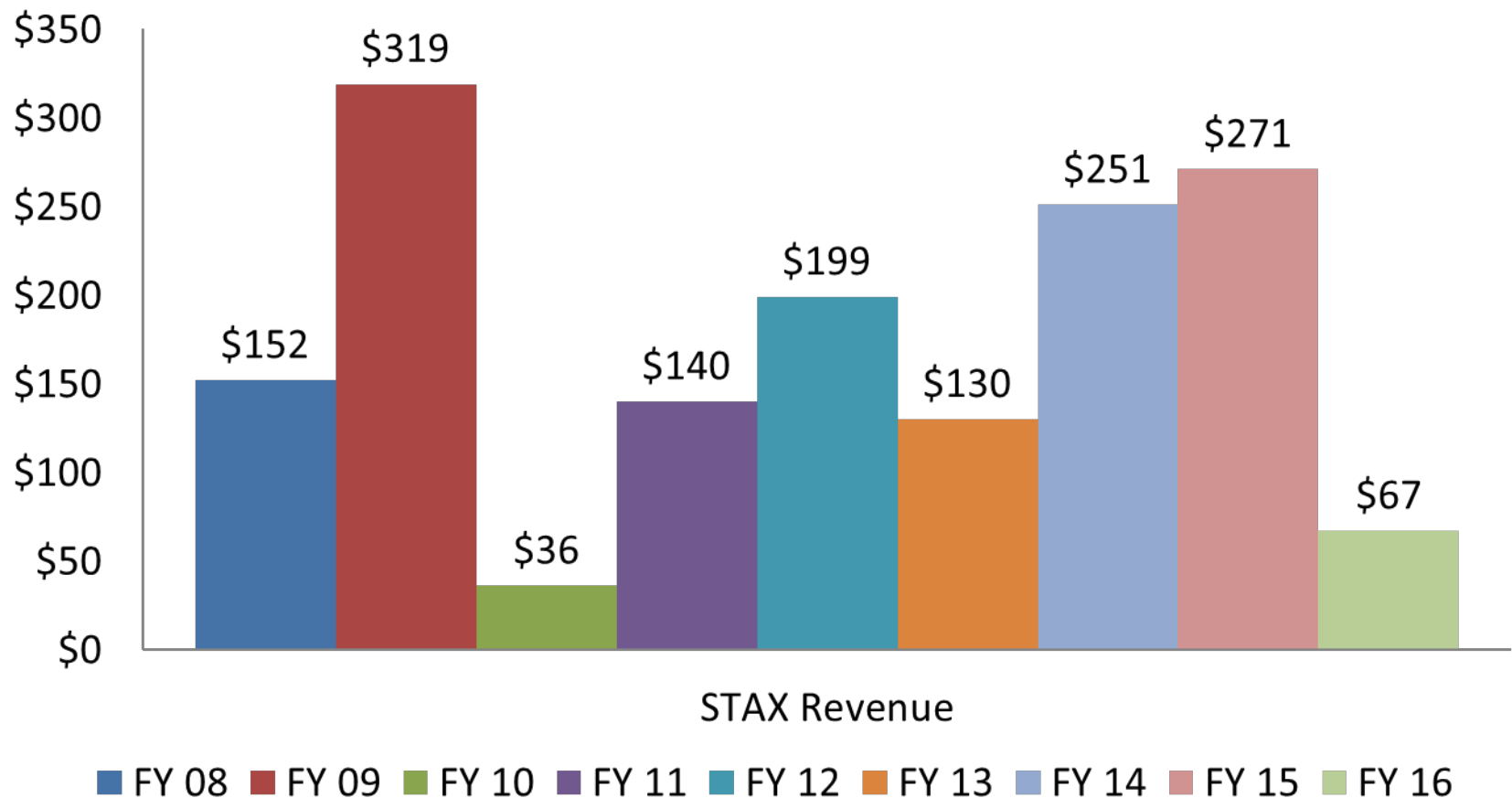
Putting It All Together: Balancing the General Fund Budget

- Transfers of cash revenues to the General Fund have also been used to balance the General Fund Budget.
- Since the Year 2000, \$167 million has been transferred out of the Perpetual Base Fund in to the General Fund. Of this amount, \$30 million was paid back in FY 2014-15. Another \$11 million will be transferred in FY 2017-18.

Putting It All Together: Balancing the General Fund Budget

- Additional transfers to the General Fund have been made from the CWCB Construction Fund (\$10 million), the Severance Tax Operational Fund (\$43 million), and the Species Conservation Trust Fund (\$4 million).
- Local Government severance tax – as well as many other cash funds – have certainly also been subject to transfers.

Putting It All Together: This Kind of Volatility Makes Managing the States TABOR Budget More Difficult



If You are Still Awake....

THANK YOU!

And I Am Happy to Answer Any Questions