MEMORANDUM

JOINT BUDGET COMMITTEE

TO	Members of the Joint Budget Committee
FROM	Amanda Bickel, JBC Staff (303-866-4960)
DATE	March 9, 2022
SUBJECT	Enterprise Status of State Institutions: Risks Associated with Capital Grants

SUMMARY

- Due to the substantial amount of one-time revenue currently available to the State, a number of higher education institutions could potentially lose their status as enterprises under TABOR due to their receipt and expenditure of capital grants. One higher education institution (Adams State University) has already lost its status as a TABOR enterprise for FY 2021-22.

- Under the provisions of Proposition 117, a statutory measure adopted by the voters in 2020, higher education institutions that lose their enterprise status might require a vote of the people to regain their status: a costly and challenging project.

- Small higher education institutions have often temporarily lost their enterprise status in the past as a result of state capital grants. This has not had significant implications for the institutions or the State, because under TABOR and implementing statutory provisions, when an entity disqualifies as an enterprise, the Referendum C cap *adjusts* by the amount of revenue that the institution earned in the prior year.

- While previous disqualifications have not created a problem, changes in enterprise status now could become a significant concern if: (1) the State is at its revenue cap (as it is now); (2) the institution remains out of enterprise status (as might be required by the provisions adopted in Proposition 117); and (3) the institution's revenue grows more quickly than the Referendum C cap (inflation + population). This could be a particular concern if a large entity--such as the community college system--loses its enterprise status and then experiences significant increases in enrollment, as has historically occurred in recessions.

- Recent calculations provided by the Office of State Planning and Budgeting raise concerns that many of the state's higher education institutions could lose enterprise status in the coming year, including, potentially, the community college system. These calculations compare the capital construction recommendations from the Capital Development Committee and the Joint Technology Committee with the most recent institutional revenue base used by the Office of the State Auditor to determine if institutions qualify for enterprise status.

OPTIONS FOR ADDRESSING

- Since Proposition 117 is a statutory provision, the General Assembly could change the law so that institutions that disqualify as enterprises do not require a vote of the people to regain enterprise status.

- As a near-term solution, staff recommends that the JBC consider substituting some ARPA Coronavirus State Fiscal Recovery Funds from the Revenue Loss Restoration Cash Fund for capital construction funds in appropriations for institutions that appear poised to lose enterprise status. This is strictly a stop-gap, since these funds are only available on a temporary basis. However, since most of the funds will now be allowed to be used for "general government services," it appears this is an option for the State and could serve as belt and suspenders to avoid the loss of enterprise status in the absence of a near-term change to proposition 117. For the institutions, ARPA revenue does not count as a state grant for TABOR enterprise purposes, as it originates as federal funds. If this option is used, staff encourages the JBC to think about setting aside an equivalent amount of General Fund revenue for addressing issues of long-term budget stability, consistent with how legislators have often described the intended purpose of the Revenue Loss Restoration Cash Fund.

- The General Assembly could consider providing less capital support for the institutions and, if desired, directing additional funds through "Step 3" of the higher education funding model, which allows for temporary allocations of funding for particular purposes. Amounts distributed as fee for service contracts do not count as state grants.

- The General Assembly could distribute capital funds more slowly or enact legislation that requires institutions to spend funds more slowly if they are at risk of losing enterprise status. Staff believes this step makes most sense if: (1) no other action is taken (such as a change to Proposition 117 provisions) that will enable institutions to easily regain enterprise status; and/or (2) it appears that an institution is likely to lose enterprise status for an extended period of time *even if* provisions enacted in proposition 117 are changed because of multi-year capital support.

While staff has engaged in discussions with OSPB around this topic, Staff believes some additional data from the Controller's Office and input from the higher education institutions may be helpful to better understand the related risks and options. Specifically, staff wishes to better understand if, even if proposition 117 provisions change, will some institutions remain outside of enterprise status <u>and</u> experience substantial overall revenue growth over multiple years? If so, what would be the scale of the impact?[1]

BACKGROUND - HISTORY OF HIGHER EDUCATION INSTITUTIONS' ENTERPRISE STATUS

Subsection (7) of Article X, Section 20, of the Colorado Constitution, the Taxpayers Bill of Rights or TABOR, limits growth in revenue to "districts" including the state government. However, it includes an exception for revenue received by government *enterprises*. An enterprise is defined as government-owned business authorized to issue its own revenue bonds and receiving under 10%of annual revenue in grants from all Colorado state and local governments combined.

---

[1] While JBC staff tracks data on budgeted sources of revenue, significant institutional revenue is off budget. While there is an existing statutory provision at 24-77-103(7), C.R.S., that requires institutions to provide quarterly data on total revenues to the JBC, no report has been submitted in recent years to staff's knowledge. Staff is working with Legislative Council Staff to solicit and examine related data.

In the early 2000s, higher education tuition growth was a concern. As described in the JBC Higher Education Budget Briefing document for FY 2008-09:

> "Prior to the higher education institutions gaining enterprise status, and prior to Referendum C, increases in higher education revenues, particularly tuition, could cause the state to be required to refund more General Fund. This reduced the General Fund available for capital construction, roads, and potentially operating expenses. In the early 2000's, when the state was reducing General Fund appropriations for higher education institutions to balance the budget within available revenues, it also limited the capacity of higher education institutions to increase tuition to compensate for the loss in General Fund. This was because any increase in tuition would have reduced the available General Fund by increasing the refund due to taxpayers."[2]

This was addressed by S.B. 04-189, which required that direct appropriations for higher education institutions be replaced by a combination of stipends for students and "fee-for-service" contracts. Senate Bill 04-189 states that stipends and fee-for-service contracts are not state grants for TABOR purposes. In the case of stipends, the payments are on behalf of students that have choice in where to apply the funds, and thus the benefit to higher education institutions is indirect. In the case of fee-for-service contracts, a market exchange occurs where services are provided and paid for at a rate sufficient for the independent operation of the enterprise. By FY 2006-07, all of the state-operated higher education institutions had been designated as enterprises.

However, not all of the state higher education institutions have *maintained* enterprise status in all years. S.B. 04-189 did not redefine the way that the State supports capital construction. Some of the state's smallest institutions have temporarily disqualified as TABOR enterprise status and then typically requalified as enterprises the next year. A memorandum published annually by the Office of the State Auditor identifies which institutions are qualified as enterprises and which are not in any given year.[3]

While stipends and fee-for-service contracts provided to students under the College Opportunity Fund program do not qualify as state grants, capital construction funding does qualify as a grant. A 2018 memorandum by Legislative Council Staff explains the process by which higher education institutions have qualified or disqualified as enterprises and the implications for the state's TABOR cap under Referendum C.[4]

> "**Qualification and disqualification**. Article X, Section 20 (7)(d) of the Colorado Constitution states that "[q]ualification or disqualification as an enterprise shall change district bases and future year limits." Implementing statute requires that the revenue limit must be adjusted for qualification and disqualification of enterprises.[5]

---

[2] FY 2008-09 Higher Education Budget Briefing, Eric Kurtz, Dec. 10, 2009, p 58.
[3] https://leg.colorado.gov/sites/default/files/documents/audits/2157s_higher_education_enterprise_memo_2021.pdf
[4] Greg Sobetski, *The TABOR Revenue Limit*, November 29, 2018 https://leg.colorado.gov/publications/tabor-revenue-limit
[5] Section 24-77-103 (1)(b) and (2.3), C.R.S.

When an existing state program qualifies as an enterprise, its revenue for the most recent fiscal year is subtracted from that year's revenue limit before inflation and population adjustments are applied:

$$\begin{pmatrix} \text{prior year limit} \\ -\text{ prior year qualifying enterprise revenue} \end{pmatrix} \times \begin{pmatrix} \text{inflation} \\ +\text{ population growth} \end{pmatrix} = \text{current year limit}$$

When an existing state program is disqualified as an enterprise, its revenue for the most recent fiscal year is added to that year's revenue limit before inflation and population adjustments are applied:

$$\begin{pmatrix} \text{prior year limit} \\ +\text{ prior year disqualified enterprise revenue} \end{pmatrix} \times \begin{pmatrix} \text{inflation} \\ +\text{ population growth} \end{pmatrix} = \text{current year limit}$$

Adjustments for qualification or disqualification of an enterprise are made if an existing program is designated as an enterprise, or if an existing enterprise is reclassified to lose that designation. Additionally, adjustments are made in years when an enterprise fails to meet statutory criteria. This most often occurs when small institutions of higher education, such as Adams State University, Fort Lewis College, or Western State Colorado University, receive state grants, e.g. for capital construction projects, that exceed 10 percent of their revenue for the fiscal year.

Adjustments for qualification of an enterprise are made when a preexisting government program is designated as an enterprise. Adjustments are not made when a brand new program is created as an enterprise."

Because the Referendum C cap is adjusted when an institution disqualifies as an enterprise, there is no immediate impact on the state's ability to retain general tax revenue when an institution disqualifies. This becomes a concern, however, if an institution is included within the state "district" for more than one year and its revenue grows more quickly than the state's allowed growth under the Referendum C cap. For example, if the community college system were to lose its enterprise status at a point when the State is at its Referendum C cap *and* the system began to experience significant enrollment increases, the revenue associated with that enrollment growth might result in refunds of general tax revenue.

Proposition 117, adopted by the voters in 2020, added the following provision to statute:

> "**24-77-108.** Creation of a new fee-based Enterprise. In order to provide transparency and oversight to government mandated fees the People of the State of Colorado find and declare that: (1) After January 1, 2021, any state enterprise qualified or created, as defined under Colo.Const. Art. X, section 20(2)(d) with projected or actual revenue from fees and surcharges of over $100,000,000 total in its first five fiscal years must be approved at a statewide general election. Ballot titles for enterprises shall begin, "SHALL AN ENTERPRISE BE CREATED TO COLLECT REVENUE

> TOTALING (full dollar collection for first five fiscal years) IN ITS FIRST FIVE YEARS...?" (2) Revenue collected for enterprises created simultaneously or within the five preceding years serving primarily the same purpose shall be aggregated in calculating the applicability of this section."

As written, this provision requires higher education institutions that lose enterprise status to obtain a vote of the people to regain such status. This would clearly be a costly and challenging project. Thus, institutions that previously lost enterprise status for a year and then regained it might instead lose their enterprise status permanently.

Staff understands that Adams State University has already lost its enterprise status for FY 2021-22 based on expenditures to-date.

DATA FROM OFFICE OF STATE PLANNING AND BUDGETING

The attached spreadsheet from the Office of State Planning and Budgeting compares the most recent data from the annual report by the Office of the State Auditor on institutional revenues and institutions' TABOR enterprise status with the recommendations from the Capital Development Committee and Joint Technology Committee. As can be seen, in this analysis, Adams State University, Colorado Mesa University, Western Colorado University, Fort Lewis College, and the community college system would all fall off enterprise status if all of the funding were approved and expended in a single year. This is also true for the Auraria Higher Education Center. Staff understands that the revenue is recognized as a state grant in the year it is expended, rather than the year in which it is appropriated. Thus the percentages may be overstated, but they still suggest that larger entities, such as the community college system, could be affected by too exuberant capital spending.

CDC and JTC Recommendations for Higher Education Institutions Compared to 2022 Revenue

OSPB-recommended projects shown in italics

Institution	Project Name	FY 2022-2023 GF (CCF)	Institution Totals	2022 Revenue	Capital to Revenue
Adams State University			$ 15,337,718	$62,163,166	25%
	Controlled Maintenance (all 3 levels)	*2,516,619*			
	Central Technology Renovation, Adams State University	7,633,103			
	Digital Transformation Initiative (w Western & FLC)	5,187,996			
Auraria Higher Education Center			$ 25,861,801	$30,400,000	85%
	Controlled Maintenance (all 3 levels)	*3,714,419*	*AHEC revenue is estimated pending confirmation from CDHE		
	Campus-wide Building Envelope and Energy Code Deficiencies (Capital Renewal), Auraria Higher Education Center	22,147,382			
Colorado Community Colleges System			$ 119,506,071	$782,947,733	15%
	LCC Bowman, Lamar Community College (Capital Renewal)	*3,944,152*			
	Freudenthal Library Renovation, Trinidad State Junior College	*1,165,125*			
	Boulder Creek Health Education Center of Excellence, Community College of Denver	*21,080,133*			
	Controlled Maintenance (all 3 levels)	*31,484,839*			
	Applied Technology Campus Expansion and Remodel, Northeastern Junior College	11,500,000			
	Dental Hygiene Growth/Expansion Project, Pueblo Community College	6,300,000			
	First Responder Emergency Education Complex, Pikes Peak Community College	33,395,759			
	Classroom & Conference Room Technology, Community College of Denver	1,532,140			
	Rural College Consortium	8,627,000			
	Improving Student Access to Technology, Community College of Aurora	476,923			
Colorado Mesa University			$ 47,542,336	$188,509,171	25%
	Controlled Maintenance (all 3 levels)	*3,954,540*			
	Replace Robinson Theater, Colorado Mesa University	39,454,194			
	ERP Modernization	4,133,602			
Colorado School of Mines			$ 17,614,284	$386,108,452	5%
	Controlled Maintenance (all 3 levels)	*3,310,132*			
	Arthur Lakes Library Renovation, Colorado School of Mines	12,000,152			
	Re-envisioning Mines ERP and SIS	2,304,000			
Colorado State University			$ 70,149,072	$1,715,397,110	4%
	NWC COP Payment, Colorado State University	*17,496,791*			
	Controlled Maintenance (all 3 levels)	*11,384,867*			
	S.B. 20-219 COP Payment, FLC, CSU, and CU	1,235,927			
	Clark Building Renovations and Additions, Colorado State University - Fort Collins	38,927,539			
	Network Hardware Upgrade	646,119			
	Communications System Upgrade	457,829			
Fort Lewis College			$ 15,293,884	$86,120,912	18%
	Berndt Hall, Fort Lewis College (Capital Renewal)	*4,200,399*			
	S.B. 20-219 COP Payment, FLC, CSU, and CU	*1,926,018*			
	Controlled Maintenance (all 3 levels)	*3,979,471*			
	Digital Transformation Initiative (w Western & Adams)	5,187,996			
Metropolitan State University			$ 14,145,000	$266,880,030	5%
	Health Institute, Metropolitan State University	10,000,000			
	Reimagining the Campus Digital Experience	3,350,000			
	Network Infrastructure Modernization	795,000			
University of Colorado			$ 52,807,130	$5,058,257,269	1%

CDC and JTC Recommendations for Higher Education Institutions Compared to 2022 Revenue OSPB-recommended projects shown in italics					
Institution	Project Name	FY 2022-2023 GF (CCF)	Institution Totals	2022 Revenue	Capital to Revenue
	Controlled Maintenance (all 3 levels)	*14,470,977*			
	S.B. 20-219 COP Payment, FLC, CSU, and CU	1,584,429			
	Hellems Arts & Sciences and Mary Rippon Outdoor Theatre Renovation, University of Colorado Boulder	10,868,038			
	CU Denver Building Infrastructure Replacement and Renovation (Capital Renewal), University of Colorado Denver	25,883,686			
University of Northern Colorado			$ 10,538,747	$246,136,825	4%
	Gray Hall, University of Northern Colorado (Capital Renewal)	*4,540,656*			
	Controlled Maintenance (all 3 levels)	*1,672,507*			
	ERP Modernization and Cloud Migration	4,325,584			
Western Colorado University			$ 10,888,254	$67,316,582	16%
	Hurst Hall Lab Renovation, Western Colorado University (Capital Renewal)	*3,831,677*			
	Controlled Maintenance (all 3 levels)	*1,868,581*			
	Digital Transformation Initiative (w FLC & Adams)	5,187,996			