

DEPARTMENT OF LOCAL AFFAIRS
JBC Budget Hearing

Monday, December 18, 2006

Introductions/Opening Comments

Brian Vogt, Executive Director

Matthew Blackmon, Budget Director

Barb Kirkmeyer, Director of Division of Local Government

George Epp, Director of Division of Emergency Management

Kathi Williams, Director of Division of Housing

The Department of Local Affairs' (DOLA) mission is to help build the capacity in local communities. We do this in two ways: Financial Assistance and Technical Assistance. These services include specialized training, technical, and financial assistance, and emergency management. Through our work with communities, the Department strives to:

- Help improve physical conditions of communities.
- Help improve leadership and governing capacities of communities.
- Help improve opportunities for eligible individuals in communities.
- Improve its internal management.

In order to accomplish this mission, DOLA's programs and services are focused on local communities. Thus, performance outcomes are mainly targeted at the local level, resulting in a statewide outcome of strong communities. Local government needs drive the activities and budget resources within the department.

From a budget perspective, 89% of the total departmental appropriation is considered "custodial" – this is defined by the department as state or federal funding that is appropriated to the department on behalf of eligible local governments to be either distributed to local governments through a formula and/or statutorily allowable granting process. This includes such programs as the Volunteer Firefighter Pension Program and the Conservation Trust Fund.

The remaining budget is appropriated as programmatic funds that can be addressed in questions one through four.

1. How do your performance measures influence department activities and budgeting?

The Department of Local Affairs overall budgetary goals influence the department's performance measures. Performance measures have a direct impact on program processes. For example, when a decision made by the Board of Assessment Appeals is reversed by the Colorado Court of Appeals, which only occurs on average one case out of every 1,280 cases decided by the Board, the

program's process will be modified to incorporate the courts decision. This has a direct impact on future Board decisions.

2. To what extent do the performance outcomes reflect appropriation levels?

In order to stay within the available appropriation, the department must determine an acceptable level for wait times and backlog of cases. Therefore, the department prioritizes activities in the following manner:

1. Constitutional requirements
2. Statutory mandates
3. Regulatory functions
4. Good business practices

An example of departmental prioritization would be if the State Board of Equalization were to order the Division of Property Taxation to conduct multiple reappraisal orders within the same fiscal year. These reappraisals would be conducted. The result would be that services such as assessor training may not be completed at the targeted level within the current fiscal year and therefore would be completed in the following fiscal year.

3. To what extent do you believe that appropriation levels in your budget could or should be tied to specific performance measure outcomes?

The appropriation levels and performance measures need to be program specific addressing statutory mandates and constitutional requirements. There is also a critical need to review the availability of cost effective program measures that can modify actions to improve outcomes. The department is willing to work with the JBC staff to determine the appropriate mix to enhance performance outcomes.

4. As a department director, how do you judge your department's performance? What key measures and targets do you use?

I utilize a combination of internal and external independent entities to judge the department's performance. I have regular internal meetings with senior staff members, employee groups, and I participate on advisory committees. I also meet with local governments and special interest organizations seeking input and recommendations on programs and services. Other independent entities may include the Colorado Court of Appeals and other state agencies (such as CDOT, Corrections, and CDPHE), that utilize the department's demographic and cartographic population estimates and forecasts.

Implementing Legislation Concerning Illegal Immigration: H.B. 06S-1023 and H.B. 06S-1009

5. Provide a list of programs in your department that are subject to the provisions of the two bills.

- a. Senior Tax Exemption (and the recently approved Disabled Veteran's Tax Exemption) program. Since the Senior Tax Exemption application deadline was prior to the passage of these bills, the department took no action for this year. Next year, the department will be revising the forms to request that assessors verify identification of applicants and provide information on the type of identification and its number, if appropriate. These forms are updated in the normal course of business. Additionally, the Senior Tax Exemption Brochure will be updated, which the department makes available to the general public and assessors. Updating this brochure is within the normal course of business.
- b. Manufactured Housing Installation Program
- c. Dealer Registration Program
- d. Factory Built Housing Program
- e. Factory Built Nonresidential Structures Program
- f. Multi-family Structures Program

6. How has your department implemented the provisions of the two bills? What problems have been encountered in implementing them?

The department has established a policy and the appropriate forms to verify the lawful presence of any individuals participating in affected programs. Implementation has not been problematic because most of the program participants are legal entities.

The department has had no serious implementation problems. However, local agencies and organizations that provide direct services to households have encountered problems with understanding and implementation of the new regulations. Additional training for line-staff at the local agencies in the various projects and programs funded through the department is necessary for consistent delivery of the intent of the bills.

7. Provide an estimate of the costs your department will incur in FY 2006-07 to implement the bills. Are any additional costs anticipated in FY 2007-08? If so, please elaborate.

The department does not anticipate additional costs associated with the implementation of the two bills. There are no additional costs anticipated in FY2007-08.

8. Provide a summary of anticipated savings in FY 2006-07 in your department as a result of not providing services to individuals who are in the country illegally. Are any additional savings anticipated in FY 2007-08? If so, please elaborate.

The department will not have savings in FY2006-07 associated with the implementation of the two bills. There are no savings anticipated in FY2007-08.

Proposal to Eliminate "Cash Funds Exempt" in the Long Bill

9. **Background.** Joint Budget Committee staff has proposed eliminating the current "Cash Funds Exempt" column in the Long Bill and replacing it with a new column entitled "Transfers" effective with the FY 2008-09 Long Bill. The Joint Budget Committee has not formally voted on this issue. For details of the proposed change, please read the Joint Budget Committee staff memo from November 15, 2006, entitled "Proposed Long Bill Format Change." To help departments understand the new format, our staff has prepared an example of the Department of Revenue FY 2006-07 Long Bill in the proposed new format. This memo, and the example from the Department of Revenue, can be downloaded from the JBC web page at the following Internet address:

http://www.state.co.us/gov_dir/leg_dir/jbc/PLBFC11-15-06.pdf

Question. Please provide the Joint Budget Committee with a summary of any potential concerns that your department may have regarding the proposed change to the Long Bill format. Please highlight potential issues such as: implementation challenges, workload issues, and other related concerns.

The Department anticipates initial accounting structural changes, but it is estimated that these changes could be absorbed within existing resources. DOLA staff will work with the JBC staff to complete the necessary changes if the JBC decides to pursue the changes in Long Bill format.

Mineral and Energy Impact Grant Program

10. Why does the Department's budget request project a \$40 million decrease in severance tax revenues between FY 2005-06 and FY 2006-07 (Schedule 11, Section 2, Page 18)? What is the Department's projection of severance tax revenues for the next few years?

The severance tax revenue estimates are based on the substantial decrease in the revenue projections provided by Legislative Council for FY2006-07. The department's allocation of severance tax was reduced proportionally.

The down turn in FY07 in the forecast is due to our projection of a decline in the price of natural gas from the high levels in 2005. It should be noted that Legislative Council and OSPB also forecast downturns in FY2007 and another in FY2008 and FY2009. The impact of this decline in price is amplified in the severance tax by the property tax credit provided in state statute.

11. Please provide some historic perspective on why the state severance tax was developed and the logic behind its relationship to local property and sales taxes. What major changes have been made to the severance tax and its distribution since the beginning of the program?

The original legislation provided a pretty clear statement of purpose for the tax:

39-29-101. Legislative declaration.

(1) The general assembly hereby finds and declares that, when nonrenewable natural resources are removed from the earth, the value of such resources to the state of Colorado is irretrievably lost. Therefore, it is the intent of the general assembly to recapture a portion of this lost wealth through a special excise tax, in addition to other business taxes, on the nonrenewable natural resources removed from the soil of this state and sold for private profit.

(2) The general assembly further finds and declares that the severance of nonrenewable resources provides a potential source of revenue to the state and its political subdivisions. Therefore, it is the intent of the general assembly to impose a tax on the process of severance in addition to other business taxes.

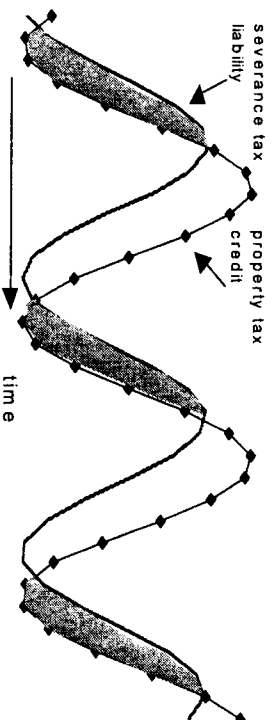
(3) It additionally is the intent of the general assembly that a portion of the revenues derived from such a severance tax be used by the state for public purposes, that a portion be held by the state in a perpetual trust fund, and that a portion be made available to local governments to offset the impact created by nonrenewable resource development.

The main source of the year-to-year variability in severance tax revenue from oil and gas is a provision in the severance tax statute (C.R.S. 39-29-105) for a property tax credit against the calculated severance tax liability. These tax

provisions amplify the effects of changes in the total annual value of oil and gas production on the resulting severance tax revenue. The severance tax statute provides for a credit against tax liability of 87.5% of local property taxes assessed during the tax year upon the production, excluding equipment and facilities. Property tax payments on oil and gas ownership in year t are based on the value assessment in year $t-1$. These, in turn, are based on the actual production quantity and price in year $t-2$. Severance tax gross liability in year t is based on production value in the same year t . Thus when a change in production value occurs it is reflected quickly in the calculation of gross severance liability, while the property tax credit that can be used by the taxpayer against this liability is based on production value two years previous. As a result, when production values increase, property tax credits lag, resulting in an amplified increase in severance tax revenues. The same type of amplification would occur with a production value decline, reducing the severance tax liability to zero.

Figure 1 shows a schematic of the lagged credit calculation on an individual taxpayer.

FIGURE 1



Since the typical property tax mill rate on the value of production by a taxpayer is higher than the severance tax rate, much of the severance tax is only paid when the taxpayer has growing production value, shown as a shaded area.

12. The Department did not include performance data for the mineral and energy impact program among its key performance measures. How should the performance of this program be measured? What performance data can the Department report about the program?

The impact program is driven by local government priorities and needs. The division assists local governments in complying with funding requirements for eligible projects. Advisory committees are in place for many programs to weigh competing local needs. Funding for this program is appropriated to the department on behalf of eligible local governments to be either distributed to local governments through a formula for the direct distribution and a statutorily

allowable granting process. Local government participation and grant applications drive the program and the outcomes are targeted to the local government needs. The department annually publishes a report on grant awards on the department's website.

13. Please provide a version of the Department's flow chart illustrating the distribution of federal mineral lease revenues that includes the actual dollars distributed in 2005 through each step of the process. (Also, please adjust the flow chart to refer to the State Public School Fund to reduce potential confusion, since there are several similarly named funds that support K-12 education.)

Please see attached flow chart.

14. When does the Department project that Colorado will begin receiving federal mineral lease revenues from oil shale? Where will these revenues be deposited and how will they be distributed? Will all of them be deposited in the special fund subject to legislative appropriation pursuant to Section 34-63-104, C.R.S.?

The department does not have any indications as to when the state will receive federal mineral lease revenues from oil shale. The determination of which of the federal mineral lease revenues are "oil shale" to be deposited in the Oil Shale Trust Fund pursuant to 34-63-104 is made by the State Treasurer on the basis of information provided by the Federal Mineral Management Service. The department has no special information on the prospects for the oil sale projects. From the news reports and discussions with the parties it would not seem that we would have significant production from the proposed oil shale projects for a decade. Therefore, only possibility for significant federal mineral lease payments to the state in the next ten years would be in bonus payments made by corporations similar to those that occurred in the mid 70's. This does not seem likely.

34-63-104. Special funds relating to oil shale lands.

(1) All moneys from sales, bonuses, royalties, leases, and rentals of oil shale lands received by the state pursuant to section 35 of the federal "Mineral Lands Leasing Act" of February 25, 1920, as amended, shall be deposited by the state treasurer into a special fund for appropriation by the general assembly to state agencies, school districts, and political subdivisions of the state affected by the development and production of energy resources from oil shale lands primarily for use by such entities in planning for and providing facilities and services necessitated by such development and production and secondarily for other state purposes.

15. Please describe how the recent increases in gas and oil activity are impacting local government infrastructure and service needs. Please estimate and describe the most urgent funding needs over the next few years and compare these to the projected available funds from severance taxes, federal mineral lease revenues, and local property taxes.

Colorado is experiencing significant mineral exploration and extraction activity, particularly in the areas of coal and natural gas resource development. Roads, water and wastewater infrastructure, communications infrastructure, public safety projects, and public facilities have been the local government's most urgent needs over the past couple of years as evidenced by the growing number of grants awards in these areas. The department would need input from local government to estimate the need in these areas.

2002 - 2006	Number of Awards	Total amount awarded
Roads	142	\$71,847, 165
Water Infrastructure	180	\$43,604,235
Wastewater projects	120	\$33,177,438
Public Safety	157	\$29,568,544
Public Facilities	301	\$85, 762, 097

Disaster Emergency Fund:

16. Please provide a table with expenditures from the Disaster Emergency Fund over the last 8 years, the current balance in the fund, and estimated expenditures for any incidents that are still open.

Please see attached table for expenditures over the past 8 years.

The chart below lists the current balance and estimated expenses within the Disaster Emergency Fund:

Executive Order	Purpose	Expiration Date	Amount Committed	Amount Expended	Committed Remaining	Fund Balance
Balance 11-30-06						8,050,272
D 001 06	Mauricio Canyon*	10/9/2006	500,000	180,343	319,657	
D 003 06	Imminent Threat	11/6/2006	358,000	51,256	306,744	
D 008 06	Preparedness 06	8/19/2006	2,000,000	244,368	1,755,632	
D 014 06	Mato Vega	3/21/2007	3,000,000	**	3,000,000	
D017 06	Tyndall	4/13/2007	400,000	**	400,000	
D017 06	Wright	4/13/2007	400,000	**	400,000	
D017 06	Jolly Mesa	4/13/2007	700,000	**	700,000	
D018 06	Douglas Flood	4/13/2007	8,000	1,711	6,289	
D021 06	Red Apple	6/13/2007	500,000	**	500,000	
					-----	-----
					7,388,322	
Uncommitted Balance						661,950

(\$240,000 from TABOR Reserve*)

** Amounts were transferred from TABOR Reserve

Uncommitted Balance

The Fund balance as of 11-30-06 was \$8,050,272, with \$7,388,322 committed to open incidents, leaving an uncommitted balance of \$661,950.

17. Should the state assume that funding will be necessary every year for the emergency response and recovery from wildfires, and therefore should the state provide an on-going appropriation for this purpose? Why has the Emergency Fire Fund created by the local governments been insufficient to respond to wildfires? What is the appropriate balance between state and local government funding for the response and recovery from wildfires?

Given the on-going drought within Colorado and the effects of the pine beetle on federal forest lands it is safe to assume funding for response to wildfires will be necessary. Wildfire activity, severity, and cost have increased significantly in recent years. These increases are due to multiple and complex factors, including an increase in the construction of homes and other facilities in forested areas, drought, and a build-up of wild land fire fuels.

