

should consider funding all or a portion of these identified capital needs through one or more bond issues. Bonding allows the City to spread the costs of the projects over their useful life. This is economically efficient, as it may allow for a greater number of actual users of the infrastructure to share in its cost. Further, because inflation in the construction industry is running ahead of inflation for the economy as a whole, getting the projects underway and completed in less time than would be done with a pay-as-you-go approach can reduce overall project costs, even when the borrowing costs are included.

The City's current debt load is an average three percent of market value, and roughly \$2,350 per capita. Roughly 50 percent of the City's debt, including enterprise revenue debt, will be retired within the next 10 years.²⁸

According to City policy, transfers out of the general fund for capital projects are based on all revenues received from the use tax and four percent of general fund revenues. These annual transfers have averaged as much as 20 percent of general fund expenditures and transfers since FY2000. Given the importance of completing many of these capital projects and other competing general fund needs, the City could reduce its gap by as much as \$10 million a year over the next five years by not paying cash and continuing its policy of transferring all of the use tax and four percent of its general fund expenditures to capital projects.

Overview: Revenue Options

Policy Options Affecting Existing Revenue Base

As discussed in the long range forecast, the City should continue to pursue opportunities that will grow its existing revenue base. Given the reliance on the sales tax, the City should pursue strategies that grow its retail base. There are several new malls and shopping areas being developed, and these will help restore more regular revenue growth to the City.

As also mentioned in the long-range forecast, over time, changes to Aurora's household characteristics may reduce real City revenues. The City should continue to develop policies that stem some of these possible future losses. Attracting additional high-income residents and shoppers is a logical strategy, which can be accomplished by focusing on high-end housing and the services and amenities valued by these residents.

Tax Policy

It is important to recognize at the outset that every tax has some negative impact on the economy. By increasing the cost for a purchased good or service, taxes change market behavior, generally resulting in a reduction in demand. The result of this market behavior, the "deadweight loss" from taxation, must be balanced against the value of the goods and services that government delivers through use of those tax revenues.

²⁸ "Aurora, Colorado," Standard and Poor's, February 2, 2006.



As revenue alternatives are analyzed and considered, the economic impact of these choices should and will be assessed. Generally, there is a preference for smaller, incremental changes in taxes as opposed to large, sweeping changes, particularly where they involve use of a new tax. One reason for favoring incremental changes is that they are less likely to result in significant changes in market patterns. With larger changes, there is a greater possibility that specific businesses or industries will be negatively impacted by the market response to a particular tax. Along the same lines, there generally is a preference for broad use of several tax methods as opposed to extensive use of only one or two taxes that may prove to be particularly burdensome to specific businesses or industries.²⁹

City revenue structures are unique to a particular community and are often driven by state and local laws and ordinance, history, and local and regional issues, including competition and intergovernmental relationships. In Colorado, they are also impacted by TABOR, which establishes specific requirements for amounts of revenue that may be raised and approval by voters for changes in the revenue structure.

Section One: General Principles of Tax Policy

There are widely diverging opinions on what constitutes good tax policy, and in many instances, politics and self-interest enter into the discussion. Various resources are available that look at the issues surrounding taxation in a relatively neutral fashion. The National Conference of State Legislatures has published one frequently cited list of “Principles of a High-Quality State Revenue System.” While the focus is on state revenues, it is a useful guide to taxation in general. Their principles are:³⁰

1. A high-quality revenue system comprises elements that are complementary, including the finances of both state and local governments.
2. A high-quality revenue system produces revenue in a reliable manner. Reliability involves stability, certainty and sufficiency.
3. A high-quality revenue system relies on a balanced variety of revenue sources.
4. A high-quality revenue system treats individuals equitably. Minimum requirements of an equitable system are that it imposes similar tax burdens on people in similar circumstances, that it minimizes regressivity, and that it minimizes taxes on low-income individuals.
5. A high-quality revenue system facilitates taxpayer compliance. It is easy to understand and minimizes compliance costs.

²⁹ Bland, Op. Cit., p.33.

³⁰ National Conference of State Legislatures, “Principles of a High-Quality State Revenue System, Fourth Edition, June 2001.



6. A high-quality revenue system promotes fair, efficient and effective administration. It is as simple as possible to administer, raises revenue efficiently, is administered professionally, and is applied uniformly.
7. A high-quality revenue system is responsive to interstate and international economic competition.
8. A high-quality revenue system minimizes its involvement in spending decisions and makes any such involvement explicit.
9. A high-quality revenue system is accountable to taxpayers.

The American Institute of Certified Public Accountants has published a Tax Policy Concept Statement that outlines their guiding principles for good tax policy. In many respects, it mirrors the NCSL principles:³¹

1. **Equity and fairness.** Similarly situated taxpayers should be taxed similarly.
2. **Certainty.** The tax rules should clearly specify when the tax is to be paid, how it is to be paid, and how the amount to be paid is to be determined.
3. **Convenience of Payment.** A tax should be due at a time or in a manner that is most likely to be convenient for the taxpayer.
4. **Economy in Collection.** The costs to collect a tax should be kept to a minimum for both the government and taxpayers.
5. **Simplicity.** The tax law should be simple so that taxpayers understand the rules and can comply with them correctly and in a cost-efficient manner.
6. **Neutrality.** The effect of the tax law on a taxpayer's decisions as to how to carry out a particular transaction or whether to engage in a transaction should be kept to a minimum.
7. **Economic Growth and Efficiency.** The tax system should not impede or reduce the productive capacity of the economy.
8. **Transparency and Visibility.** Taxpayers should know that a tax exists and how and when it is imposed upon them and others.
9. **Minimum Tax Gap.** A tax should be structured to minimize noncompliance.
10. **Appropriate Government Revenues.** The tax system should enable the government to determine how much tax revenue will likely be collected and when.

It is also useful to compare principles among groups with difference general views on tax policy. The Tax Foundation, generally considered a conservative tax think tank, lists the following as its "Ten Principles of Sound Tax Policy:"³²

1. Transparency is a must
2. Be neutral
3. Maintain a broad base

³¹ "Guiding Principles of Good Tax Policy: A Framework for Evaluating Tax Proposals," American Institute of Certified Public Accountants, 2001, p. 9-10.

³² The Tax Foundation, "Ten Principles of Sound Tax Policy,": <http://www.taxfoundation.org>



4. Keep it simple
5. Stability matters
6. No retroactivity
7. Keep tax burdens low
8. Don't inhibit trade
9. Ensure an open process
10. State and local taxes matter.

The Institute on Taxation and Economic Policy, generally considered a liberal think tank, has published their own assessment. They identify the following as the building blocks of a sound tax system:³³

1. Maintain vertical equity (tax systems should not be regressive)
2. Maintain horizontal equity (taxpayers in similar circumstances should pay similar amounts of tax)
3. Adequacy (raises enough funds to sustain the level of services demanded by citizens)
4. Simplicity
5. Exportability (individuals and businesses from other locations that enjoy public services should help pay for them)
6. Neutrality (tax system should stay out of the way of economic decisions).

Finally, Robert Bland identifies the three criteria that should guide local government revenue policy making. These fall into three broad categories, which he refers to as “the pillars of support for a sound local economy.”³⁴

1. Equity (the fair distribution of both the tax burden and the benefits from public services)
2. Neutrality (provide the least interference by taxes in the marketplace)
3. Effective administration (take into account the cost to government to administer the tax or cost to taxpayers to comply with the tax)

While there is some variation in the terminology, there are some clear principles that emerge where there is close to complete agreement. These principles are:

1. The system should minimize interference by taxes in market decisions
2. The system should be reliable, stable, and sufficient
3. The system should be simple, allow for compliance and easy administration
4. The system should be equitable
5. The system should have a balanced variety of sources/broad base

In particular, there was remarkably similar discussion and belief in the value of the first principle. It is also notable that the original City of Aurora Request for Proposal required

³³ The Institute on Taxation and Economic Policy, “Tax Principles: Building Blocks of a Sound System,” p. 1-2.

³⁴ Robert L. Bland, “A Revenue Guide for Local Government Second Edition, ICMA, 2005, p. 21



that “the impact of current revenue streams and revenue enhancements on citizens, businesses, and developers must be addressed.”³⁵ This will be an important area of focus when analyzing specific options.

Because Bland’s analysis focuses specifically on local revenue systems, he identifies some useful areas where local revenue structures may be somewhat different from federal or state systems. In this analysis, he reaches the following conclusions, which will be assessed in the revenue recommendations in the next chapter:³⁶

- When in doubt, use benefits based levies
- Broad-based taxes and a flat rate are less distorting to the local economy
- Consumption and income-based taxes should be assessed on potential for border-city effects
- Avoid imposing corporate income taxes or gross receipts taxes on business sales
- Any tax on business should be widely used in the State or region
- Taxes on the less mobile components of production (land, buildings, equipment) have the least detrimental effect on markets
- Eliminate nuisance taxes that have low revenue yields and high administrative and/or compliance costs
- Excise taxes, especially “sin” taxes and those borne by nonresidents usually arouse the least opposition

Section Two: Taxes in Colorado and the United States

Colorado’s tax system is different in many respects from the nation as a whole, and this has important implications for comparisons of Colorado cities’ revenues and expenditures with other cities around the country. While in most states, the majority of state and local revenue is collected at the state level, the opposite is true for Colorado. In Colorado, 46 percent of revenue is raised at the state level and 54 percent at the local level. The national average is 54.9 percent raised at the state level and 45.1 percent at the local level.³⁷

Colorado is one of only five states where local revenue collections are greater than state revenue collections. While New York is only slightly behind Colorado for the lead in local revenue generation, it is notable that New York Counties share responsibility with the State for funding of Medicaid, which is one of the larger areas for expenditure by State governments across the Country.

Colorado also collects relatively little in State taxes as a share of personal income. In 2004, Colorado had the lowest state tax collections (\$44.57) per \$1,000 of personal income of all the 50 States. Colorado’s tax burden has declined by \$7.84 over the past

³⁵ City of Aurora, “R-1259 Study of City Revenues for the City of Aurora, Colorado,” p.4

³⁶ Op cit., Bland, p.24-33.

³⁷ Federation of Tax Administrators, U.S. Census Bureau Census of Governments 2002. The complete listing for all states is found in the Appendix.



three years. Nationally, the average tax burden decreased by \$2.94 over the past three years. Colorado's State tax burden was 30 percent below the national average (\$63.70). The following indicates the State's ranking in selected state taxes:³⁸

Table 20
Colorado's Rank in Selected State Taxes per \$1,000 Income, 2003-04

| Tax | Colorado | | National | |
|-------------------|----------|---------|----------|---------|
| | Rank | Tax | High | Low |
| Total Taxes | 50 | \$44.57 | \$100.07 | \$44.57 |
| Individual Income | 27 | \$21.68 | \$41.65 | \$0.00 |
| Sales/Use | 44 | \$12.11 | \$49.40 | \$0.00 |
| Corporate Income | 42 | \$1.51 | \$15.74 | \$0.00 |
| Gas | 34 | \$3.81 | \$8.35 | \$0.76 |
| Liquor/Tobacco | 50 | \$0.61 | \$3.67 | \$0.61 |

By contrast, Colorado's local tax burden ranks as the 12th highest in the nation. Nationally, the largest single source of tax revenue for cities is the property tax. By contrast, Colorado cities are much more dependent on the sales tax:³⁹

Table 21
National and Colorado Cities Source of Revenue

| Source | U.S Percent | Colorado Percent |
|----------------------------------|----------------|---------------------|
| Intergovernmental revenue | 25.2% | 8.9% |
| Property taxes | 17.3% | 6.0% |
| Sales and gross receipts taxes | 10.5% | 27.9% |
| Other taxes | 7.8% | 3.5% |
| Current charges | 15.4% | 22.1% |
| Miscellaneous revenue | 8.4% | 11.9% |
| Utility and liquor store revenue | 16.4% | 19.5% |
| Employee retirement revenue | -1.0% | 0.3% |
| Total | 100.0% | 100.0% |

³⁸ Tom Dunn, "How Colorado Compares in State and Local Taxes," Colorado Legislative Council Staff Issue Brief, January 24, 2005, p. 1.

³⁹ U.S. Census Bureau, "2002 Census of Governments, Volume 4, Number 5, Government Finances, p. 174.



In fact, Colorado’s local sales tax collection is among the highest in the country:⁴⁰

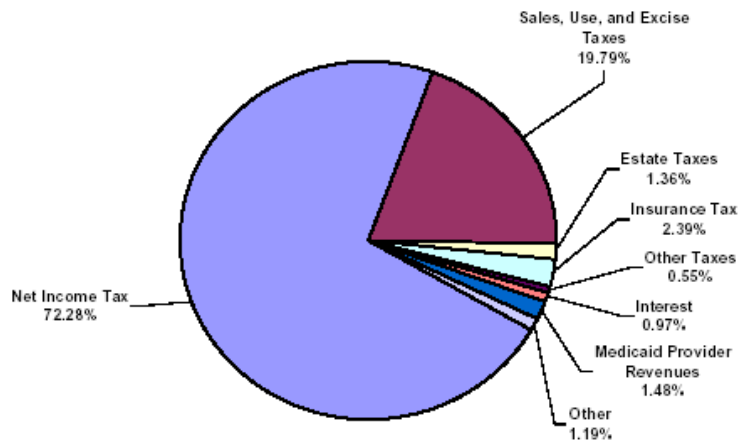
Table 22
Local Taxes as a Share of \$1,000 Personal Income, 2001-02

| | Colorado | | National | |
|-------------|----------|---------|----------|---------|
| | Rank | Tax | High | Low |
| Total Taxes | 12 | \$45.69 | \$67.19 | \$19.82 |
| Sales/Use | 2 | \$14.57 | \$22.74 | \$0.00 |
| Property | 30 | \$27.25 | \$53.10 | \$8.29 |

In general, the best way to assess a state and local tax system is to combine them, as the relationship between state and local revenues and expenditures varies widely from state to state. When viewed on a combined basis, Colorado still comes across as a low tax state, ranking 47th at a combined 9.1 percent of personal income. By contrast, the national average is 10.4 percent.⁴¹

The State of Colorado’s reliance on net income taxes is striking, making up nearly three-fourths of its general purpose revenues. When combined with sales, use, and excise taxes, these sources make up over 93 percent of general purpose revenues. The following illustrates this break down:⁴²

Figure 16
State General Purpose Revenue by Source, FY 2002



⁴⁰ Op. Cit., Dunn, p. 2.

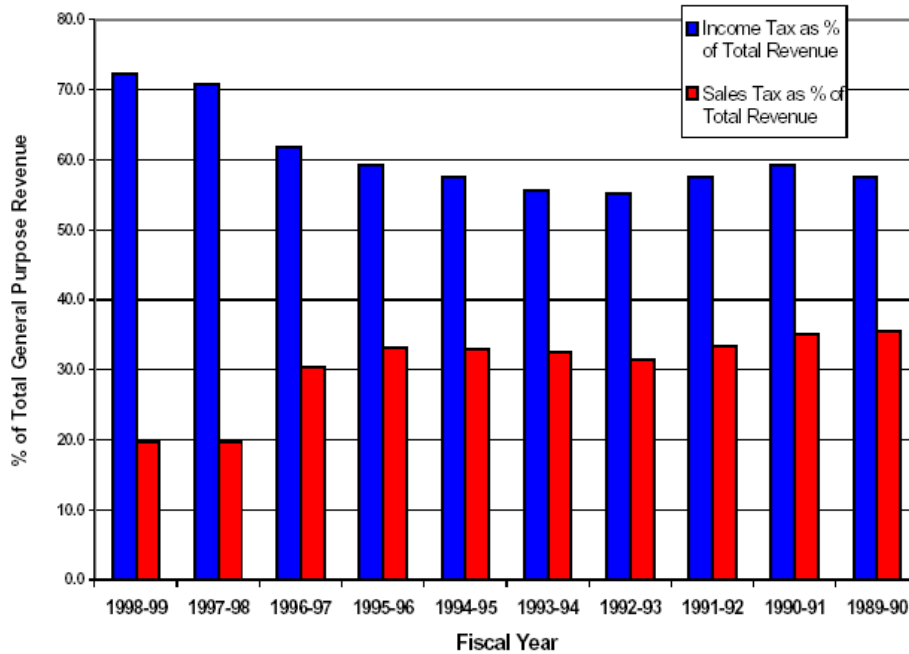
⁴¹ Op. Cit., Federation of Tax Administrators and U.S. Census Bureau Census of Governments

⁴² Daphne Greenwood and Tom Brown, “An overview of Colorado’s state and local tax structures,” Center for Colorado Policy Studies, 2002.



Greater reliance on income tax – and a reduced reliance on sales tax revenues -- were particularly pronounced in Colorado during the 1990s:⁴³

Figure 17
Colorado Sales and Income Tax as a Share of Total Revenue



When looking at the make-up of Colorado’s revenue mix, combined state and local collections are generally similar to national averages, although general sales taxes are somewhat higher and selective sales taxes somewhat lower:⁴⁴

Aurora and Comparable Cities

While Aurora’s revenue structure is not dissimilar from other Colorado cities, there are some slight areas of variation. When looking at other cities in the region (specifically; Arvada, Centennial, Colorado Springs, Lakewood, and Westminster) and all Colorado cities as a whole, Aurora’s property, sales tax, and employment occupation revenues tend to be higher, while its licenses, permits, and fees and intergovernmental revenue tends to be lower. The following table provides detail on various sources as a percent of municipal government revenues in 2002:⁴⁵

⁴³ Ibid.

⁴⁴ Op Cit., Federation of Tax Administrators. The rankings for each State can be found in the appendix.

⁴⁵ Colorado Division of Local Government, April 27, 2005, p. 338.

