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Fiscal Note

Drafting Number: LLS 21-0743
Prime Sponsors: Rep. Woog
Sen. Kirkmeyer

Date: March 24, 2021
Bill Status: House Finance
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Bill Topic: **INCOME TAX CREDIT FOR INCOME TAXES PAID**

Summary of Fiscal Impact:

<input checked="" type="checkbox"/> State Revenue	<input type="checkbox"/> TABOR Refund
<input checked="" type="checkbox"/> State Expenditure	<input type="checkbox"/> Local Government
<input type="checkbox"/> State Transfer	<input type="checkbox"/> Statutory Public Entity

For tax years 2021 through 2025, the bill creates a state income tax credit for taxpayers with taxable incomes below \$20,000, or \$40,000 if filing jointly, effectively offsetting the amount of state income tax they would otherwise owe. It decreases state revenue and increases state expenditures through FY 2025-26.

Appropriation Summary: For FY 2021-22, the bill requires an appropriation of \$258,096 to the Department of Revenue.

Fiscal Note Status: This fiscal note reflects the introduced bill.

Table 1
State Fiscal Impacts Under HB 21-1197

		Current Year FY 2020-21	Budget Year FY 2021-22	Out Year FY 2022-23
Revenue	General Fund	(\$181 million)	(\$363 million)	(\$367 million)
	Total	(\$181 million)	(\$363 million)	(\$367 million)
Expenditures	General Fund	-	\$258,096	\$289,673
	Centrally Appropriated	-	\$42,542	\$64,534
	Total	-	\$300,638	\$354,207
	Total FTE	-	2.9 FTE	4.4 FTE
Transfers		-	-	-
TABOR Refund		-	-	-

Summary of Legislation

For tax years 2021 through 2025, the bill creates a state income tax credit for Colorado taxpayers with federal taxable incomes of less than:

- \$20,000 for individual taxpayers; or
- \$40,000 for taxpayers filing jointly.

The amount of the tax credit is equal to the amount of state income tax owed, such that the credit effectively reduces state income tax liability to \$0. No excess amount may be refunded or carried forward to a future year. A taxpayer must file a state income tax return in order to claim the credit.

State Revenue

The bill decreases General Fund revenue by an estimated \$181 million in the current FY 2020-21, \$363 million in FY 2021-22, and \$367 million in FY 2022-23. The estimate for FY 2020-21 represents a half-year impact for tax year 2021 on an accrual accounting basis. The bill is expected to decrease revenue through FY 2025-26. It decreases state income tax revenue, which is subject to TABOR.

Assumptions. Table 2 shows the number of taxpayers expected to qualify for the tax credit in 2021 and the revenue impact of allowing the credit to each group of taxpayers. Populations are based on data reported by the Department of Revenue for tax year 2019 and grown to account for the change in population between 2019 and 2021. Data were also adjusted to account for the decrease in the state income tax rate beginning in tax year 2020 under Proposition 116. The bill is expected to allow a credit to roughly 21 percent of taxpayers filing Colorado income tax returns. Tax returns with taxable income of \$0 are omitted from the analysis, as taxpayers filing such returns are not expected to claim the credit.

Table 2
HB 21-1197 Tax Credit Assumptions for Tax Year 2021

Filing Status	Number of Returns	Taxable Income	Revenue Decrease from Tax Credit
Single,* with taxable income below \$20,000	532,000	\$4.67 billion	(\$211 million)
Joint, with taxable income below \$40,000	186,000	\$3.33 billion	(\$150 million)
Total	718,000	\$8.00 billion	(\$361 million)

**Includes taxpayers filing as individuals, heads of household, and married taxpayers filing separately.*

Estimates for the revenue impact of the tax credit are slightly less than 4.55 percent of estimated taxable income due to the availability of other credits for some taxpayers. The estimates in Table 1 convert tax year basis estimates to fiscal year basis estimates, such that the estimate for the current FY 2020-21 represents a half-year impact for tax year 2021, the estimate for FY 2021-22 represents half-year impacts for each of tax years 2021 and 2022, and so on.

State Expenditures

The bill increases General Fund expenditures by an estimated \$300,638 and 2.9 FTE in FY 2021-22, and by \$354,207 and 4.4 FTE in FY 2022-23 and future fiscal years. Expenditures are expected to increase through FY 2025-26. Expenditures are summarized in Table 3 and explained below.

**Table 3
 Expenditures Under HB 21-1197**

	FY 2021-22	FY 2022-23
Department of Revenue		
Personal Services	\$149,670	\$226,950
Operating Expenses	\$4,455	\$5,940
Capital Outlay Costs	\$31,000	-
Computer Programming and Testing	\$17,278	-
Data Analysis and Reporting	\$800	\$1,600
Document Management and Form Changes	\$54,893	\$55,183
Centrally Appropriated Costs ¹	\$42,542	\$64,534
Total Cost	\$300,638	\$354,207
Total FTE	2.9 FTE	4.4 FTE

¹ Centrally appropriated costs are not included in the bill's appropriation.

Department of Revenue. Most costs in Table 3, including those for personal services, operating expenses, capital outlay costs, and centrally appropriated costs, are for the addition of 2.9 FTE in FY 2021-22 and 4.4 FTE in FY 2022-23 and subsequent years in the department's Taxpayer Service section and Tax Audit and Compliance section. First-year costs are prorated for the General Fund pay date shift and a November 1, 2021, start date. These personnel are required to review tax returns claiming the credit that include mathematical or substantive errors. About 10 percent of returns are expected to have mathematical errors, of which 10 percent will require review. Less than 2 percent of returns are expected to have substantive errors, of which 50 percent will require review, correspondence with the taxpayer, or both. The estimated shares of filings that will be incorrect are based on observed rates for other nonrefundable tax credits.

Expenditures also include programming and testing of the credit in the department's GenTax software system and reporting and analysis of data related to the credit in the department's Office of Research and Analysis.

Finally, the bill will increase workload to process paper tax returns on which the credit is claimed. Approximately 11 percent of taxpayers file returns on paper. Paper returns are processed by the Department of Personnel and Administration's Integrated Document Solutions subgroup, and paid using reappropriated Department of Revenue funds.

Centrally appropriated costs. Pursuant to a Joint Budget Committee policy, certain costs associated with this bill are addressed through the annual budget process and centrally appropriated in the Long Bill or supplemental appropriations bills, rather than in this bill. These costs, which include employee insurance and supplemental employee retirement payments, are estimated to be \$42,542 in FY 2021-22 and \$64,534 in FY 2022-23 and subsequent years.

TABOR refunds. The bill decreases state revenue subject to TABOR. The March 2021 LCS forecast projects that revenue will fall short of the TABOR limit through at least FY 2022-23, though revenue expectations are close enough to the limit that a refund obligation is possible within normal forecast error. If actual revenue would exceed the limit under current law, the bill will decrease the amount required to be refunded to taxpayers. If the bill causes revenue to fall below the limit by \$30 million or more in FY 2022-23 and subsequent years, it will trigger annual transfers of up to \$30 million from the Unclaimed Property Trust Fund to the Housing Development Grant Fund under current law enacted in House Bill 19-1322.

Effective Date

The bill takes effect 90 days following adjournment of the General Assembly sine die, assuming no referendum petition is filed.

State Appropriations

For FY 2021-22, the bill requires a General Fund appropriation of \$258,096 to the Department of Revenue, with an allocation of 2.9 FTE. From this amount, \$54,893 should be reappropriated to the Department of Personnel and Administration.

State and Local Government Contacts

Personnel

Revenue