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FISCAL NOTE

Drafting Number: LLS 20B-0044
Prime Sponsors: Rep. Soper; Rich Sen. Tate
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Bill Status: House SVMA
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Bill Topic: TIPS & GRATUITIES TAX DEDUCTION

Summary of Fiscal Impact:

- State Revenue
- State Expenditure
- State Transfer
- TABOR Refund
- Local Government
- Statutory Public Entity

This bill allows taxpayers to deduct all tip income from their taxable income for the 2021 tax year only. It requires one-time implementation expenditures and reduces General Fund revenue in FY2020-21 and FY2021-22.

Appropriation Summary: For FY 2021-22, this bill requires a General Fund appropriation of \$325,126 to the Department of Revenue.

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

**Table 1
State Fiscal Impacts Under HB 20B-1020**

		FY 2020-21 <i>(current year)</i>	FY 2021-22	FY 2022-23
Revenue	General Fund	(\$22.7 million to \$29.7 million)	(\$22.7 million to \$29.7 million)	-
	Total	(\$22.7 million to \$29.7 million)	(\$22.7 million to \$29.7 million)	-
Expenditures	General Fund	-	\$325,126	-
	Centrally Appropriated	-	\$87,476	-
	Total	-	\$412,602	-
	Total FTE	-	4.1 FTE	-
Transfers	General Fund	\$1.7 million to \$2.2 million	\$1.7 million to \$2.2 million	-
	State Education Fund	(\$1.7 million to \$2.2 million)	(\$1.7 million to \$2.2 million)	-
	Total	\$0	\$0	-
TABOR Refund		-	-	-

Summary of Legislation

For tax year 2021, this bill allows taxpayers to deduct all tip income from their federal taxable income for purposes of calculating their Colorado taxable income.

Background

Colorado imposes an income tax at a rate of 4.55 percent on the taxable income of individuals and corporations. Colorado taxable income is equal to federal taxable income as modified by additions and subtractions in Colorado law.

Assumptions

This analysis is based on 2019 Colorado employment and wage data from the Bureau of Labor Statistics for the following occupations: waiters, bartenders, dining room attendants and bartender helpers, cooks, hosts, fast food and counter workers, barbers, beauty salon and nail workers, bellhops, tour and travel guides, gambling dealers, and taxi/limousine drivers. Based on this data, this fiscal note assumes approximately 178,000 taxpayers will be eligible for this bill's deduction. Total income for each occupation was calculated based on total employment and average annual wages by occupation.

These income estimates were adjusted to account for the anticipated ongoing effects of the COVID-19 pandemic on the leisure and hospitality industry through 2021, ranging from a 15 percent to a 35 percent reduction in income across the occupations included in this analysis. A range is utilized to account for the significant uncertainty regarding the path of the recovery for the leisure and hospitality industry in 2021. This range is based on data from OpenTable, which shows that Colorado restaurants saw an approximate 37 percent decline in in-restaurant patronage between June 1, 2020 and November 26, 2020, compared to the same period in 2019.

Research from Pay Scale was used to adjust each occupation's income estimates to reflect tip income only, as the bill only allows for tip income to be deducted from taxable income. The percent of income generated from tips varies greatly by occupation, ranging from 59 percent for gambling dealers to 6 percent for fast food and counter workers.

Finally, total tip income is multiplied by the new income tax rate in 2021 (4.55 percent) to arrive at the estimated state revenue impact for this bill.

State Revenue

This bill reduces General Fund Revenue by an estimated \$22.7 million to \$29.7 million in each of FY 2020-21 and FY 2021-22.

For the 2021 tax year, the bill will reduce taxable income by between \$1.0 billion to \$1.3 billion based on the assumptions used in this analysis. Due to the difference in timing between the fiscal year and calendar year, this represents a reduction in taxable income of between \$500 and \$650 million on an accrual accounting basis in both FY 2020-21 and FY 2021-22. This reduction in taxable income amounts to a reduction in income tax revenue of \$22.7 million to \$29.7 million in both FY 2020-21 and FY 2021-22.

State Transfers

This bill reduces taxable income, which reduces the amount transferred from the General Fund to the State Education Fund under Amendment 23 by between \$1.7 million and \$2.2 million in each of FY 2020-21 and FY 2021-22.

State Expenditures

This bill increases General Fund expenditures by \$412,602 in FY 2021-22. These costs are summarized in Table 2 and explained below.

Table 2
Expenditures Under HB 20B-1020

	FY 2020-21 <i>(current year)</i>	FY 2021-22	FY 2022-23
Department of Revenue			
Personal Services	-	\$214,583	-
Operating Expenses	-	\$6,210	-
Capital Outlay Costs	-	\$37,200	-
Audit and Compliance Costs	-	\$9,790	-
Computer Programming	-	\$11,800	-
Data Management and Reporting	-	\$1,600	-
Document Management	-	\$43,943	-
Centrally Appropriated Costs*	-	\$87,476	-
Total Cost	-	\$412,602	-
Total FTE	-	4.1 FTE	-

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

Personal services. This bill will temporarily increase tax examiner workload in the Tax Auditing and Compliance Division of the Department of Revenue (DOR) in FY 2021-22. The new tax deduction for tip income will spur additional taxpayer compliance investigations. This fiscal note assumes that 10 percent of returns claiming the deduction will need to be reviewed by tax examiners, or about 18,000 returns.

Audit and compliance costs. Due to the increased audit and compliance workload, additional expenditures of \$9,790 are required for postage to communicate with taxpayers.

Computer programming. This bill requires expenditures of \$11,800 for the DOR to program and test changes to its GenTax software system. Programming will cost \$9,000, representing 40 hours of programming at a rate of \$225 per hour. All programming changes are tested by department staff. Testing for this bill will require expenditures for contract personnel totaling \$2,800 representing 50 hours of testing at a rate of \$32 per hour.

Data management and reporting. Costs for database management and reporting in the DOR's Office of Research and Analysis are estimated at \$1,600 in FY 2021-22.

Document management. The bill will require changes to tax forms and will create additional workload to prepare, scan, and enter data for paper returns claiming the new deduction, resulting in increased expenditures of \$43,943. DOR imaging and scanning services are contracted through the Department of Personnel and Administration and paid with reappropriated General Fund moneys.

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 \$87,476 in FY 2021-22.

TABOR refund. According to the September 2020 LCS Economic and Revenue Forecast, the state is not expected to collect revenue above the TABOR limit in either FY 2020-21 or FY 2021-22, and refund obligations are not anticipated for these years. This bill does not change these expectations concerning refunds to taxpayers.

Effective Date

The bill takes effect upon signature of the Governor, or upon becoming law without his signature.

State Appropriations

For FY 2021-22, this bill requires a General Fund appropriation of \$325,126 to the Department of Revenue and 4.1 FTE. Of this amount, \$43,943 will be reappropriated to the Department of Personnel and Administration.

State and Local Government Contacts

Information Technology

Personnel

Revenue