HB09-1001

Colorado Legislative Council Staff Fiscal Note

STATE
REVISED FISCAL IMPACT

(replaces fiscal note dated February 2, 2009)

Drafting Number:	LLS 09-0395	**Date:**	March 10, 2009
Prime Sponsor(s):	Rep. Rice Sen. Heath	**Bill Status:**	Senate Business, Labor and Tech.
		Fiscal Analyst:	Natalie Mullis (303-866-4778)

TITLE: CONCERNING THE CREATION OF AN INCOME TAX CREDIT TO INCENTIVIZE COLORADO JOB GROWTH.

Fiscal Impact Summary	FY 2009-2010	FY 2010-2011	FY 2011-2012
State Revenue General Fund - Income Taxes /A	($2.9 Million)	($8.6 Million)	($13.8 Million)
State Expenditures General Fund	$47,796 /B	$0	$0
FTE Position Change	0.0 FTE	0.0 FTE	0.0 FTE
Effective Date: August 4, 2009, assuming the General Assembly adjourns as scheduled and unless a referendum petition is filed. Credits are effective for tax years 2009 through 2018. The bill is repealed on January 1, 2025.			
Appropriation Summary for FY 2009-2010: None required.			
Local Government Impact: None.			

This note has been revised to incorporate amendments adopted in the House.

/A Because the degree to which jobs may be created expressly due to the bill is unknown, the fiscal impact stated above does not incorporate increased revenue from potential job creation. To the extent that this tax credit is the sole determining reason that jobs are created in the state, sales and income tax revenue from those jobs would serve to partially offset the estimated loss of state revenue.

/B This amount may be funded by line item in the FY 2009-10 Long Bill for programming costs in the Department of Revenue for 2009 legislation.

Summary of Legislation

HB 09-1001 provides an income tax credit to firms that create jobs in Colorado. If the jobs are created within an enhanced rural enterprise zone, firms must create at least 5 jobs and retain them for one year. If the jobs are not being created within an enhanced rural enterprise zone, at least 20 jobs must be created and retained for one year. In order to qualify for the credit, the jobs must bring wages of at least 110 percent of the average wage of the county in which the new jobs are located.

The tax credit, effective for tax years 2009 through 2018, is equal to one-half of the amount the employer is required to pay in federal social security and Medicare taxes on the created jobs. In most cases, this is equal to 3.825 percent of each job's annual wage. For each job created, firms receive the credit each year the job is retained for up to five years, but no later than tax year 2018. Each year's credit may be carried forward for ten years, or through tax year 2024, and is non-refundable. The bill allows the credit to be given for jobs in any industry.

Firms are required to file an initial application to the Colorado Economic Development Commission (commission) outlining the number of jobs they expect to create over a period of up to five years and must provide documentation indicating that, if not for the credit, the jobs would have been created in a competing state. Once an initial credit application has been approved, firms are required to file an annual application for each year's credit with documentation on the actual number of jobs created and retained during that year. Each year, the commission is required to issue a tax credit certificate in the amount of the credit for that year to the firm, who in turn must submit the certificate with its income tax return to the Department of Revenue. No firm may receive more in tax credits than was initially agreed upon by the commission.

The bill grants the commission authority to deny any initial application. In addition, the commission is authorized to audit the accounts of each firm within twelve months following the receipt of the credit by the firm. The commission is required to provide annual reports on the credits granted and claimed to the House and Senate Finance Committees and to share information with the Department of Revenue about each taxpayer for which they approved a credit.

State Revenue

General Fund revenue will be reduced $2.9 million in FY 2009-10, $8.6 million in FY 2010-11, and $13.8 million in FY 2011-12. It is estimated that the credit will be given to approximately 33 new firms annually for the creation of about 1,900 jobs each year. This represents 0.3 percent of the approximately 600,000 jobs created each year in Colorado. These estimates were calculated based on the performance of similar tax credits offered in Illinois, Iowa, and Oregon. It is important to note that a firm's federal tax liability may be increased as a result of this tax credit.

Because the credit can only be approved after an employee has spent a year on the job, it is assumed that no credits will be redeemed until tax year 2010 and there would be a half-year impact of $2.9 million in FY 2009-10. As shown in Table 1, the revenue impact will be phased in over five fiscal years because most jobs affected by the bill will receive a credit for multiple tax years. An average wage of approximately $38,000 in enhanced rural enterprise zones and $82,000 in the remainder of the state was assumed for jobs eligible to receive the credit in 2009.

Table 1. Five-Year Phase-In of Revenue Impact

Fiscal Year	General Fund Revenue Impact
FY 2009-10	($2.9 million)
FY 2010-11	($8.6 million)
FY 2011-12	($13.8 million)
FY 2012-13	($18.1 million)
FY 2013-14	($21.3 million)

Because the degree to which jobs may be created expressly due to the bill is unknown, the fiscal impact stated above does not incorporate increased revenue from potential job creation. To the extent that the tax credit is the sole determining reason that jobs are created in the state, sales and income tax revenue from those jobs would serve to partially offset the estimated loss in state revenue.

However, most studies indicate that taxes are but one factor of many, rather than the determining factor, that businesses use when making their relocation or expansion decisions. Factors that are consistently among those considered most important include the cost and availability of labor, land, and materials, and the quality of local transportation and energy infrastructure. In addition, firms can often realize a savings from locating near other firms in their industry and many firms consider an area's quality of life to be important. For example, PriceWaterhouseCoopers states that:

> Among those expanding, clearly the most important factors in location decisions are labor availability and productivity (cited by 60%) and favorable operating costs (58%). And, to a lesser degree, "Trendsetter" companies are motivated by: following customer or client opportunities (38%), transportation access (35%), physical viability of the site (33%), and infrastructure capacity (31%).[1]

At best, tax incentives appear to make the difference only in situations where two sites are equally desirable for other reasons and the tax situation is better on the margin at one location. According to a study that reviewed over 300 pieces of literature examining the effectiveness of state tax incentives, the tax literature indicates that when a business makes its location decision "taxes...seem to enter decisions at the very last stage, if at all."[2] After analyzing the impact of their job tax credit program, the Washington State Department of Revenue reported the following:

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1 "Trendsetter Baromer," *PriceWaterhouseCoopers Barometer Surveys*, September 30, 2002.

2 Buss, Terry F., "The Effect of State Tax Incentives on Economic Growth and Firm Location Decisions: An Overview of the Literature," *Economic Development Quarterly*, Vol. 15, No. 1, February 2001.

There appears to be little correlation between the amount of tax benefit received by participants in the tax incentive programs and the growth in employment which resulted. Therefore, these tax incentives may not be a major factor in influencing the location process for businesses.

State Expenditures

Department of Revenue: $47,796 in FY 2009-10. The Department of Revenue will incur additional information technology costs to adjust the state's current and future computer systems and forms for the new credit. The annual Long Bill may include line item funding for information technology costs associated with new legislation. While the department identified additional need for postage, taxpayer services, and tax conferees, these costs are assumed to be minimal because of the limited number of tax credit certificates expected to be received each year by the Department.

It is assumed that the **Office of Economic Development** will implement the bill within existing resources.

Other State Impacts

Based on the December 2008 Legislative Council Staff revenue forecast, there is insufficient revenue in the General Fund to allow General Fund appropriations to increase by the maximum allowable growth rate of 6 percent in FY 2009-10. By reducing General Fund revenue, this bill will reduce the amount of money available for General Fund appropriations in FY 2009-10 by $2.9 million.

Departments Contacted

Governor - Office of Economic Development   Revenue