SB13-001

Colorado Legislative Council Staff Fiscal Note

STATE
CONDITIONAL FISCAL IMPACT

Note: This fiscal note is provided pursuant to Joint Rule 22 (b) (2) and reflects strike-below Amendment L.005.

Drafting Number:	LLS 13-0419	**Date:**	April 1, 2013
Prime Sponsor(s):	Sen. Kefalas; Morse Rep. Kagan	**Bill Status:**	Senate SVMA
		Fiscal Analyst:	Ron Kirk (303-866-4785)

TITLE: CONCERNING INCOME TAX CREDITS TO SUPPORT WORKING FAMILIES, AND, IN CONNECTION THEREWITH, ENACTING THE "COLORADO WORKING FAMILIES ECONOMIC OPPORTUNITY ACT OF 2013".

Fiscal Impact Summary	FY 2013-2014	FY 2014-2015	FY 2015-2016
State Revenue General Fund - reduction*	($40.1 million)	($88.0 million)	($104.1 million)
State Expenditures General Fund*	$0.7 million	$1.7 million	$1.6 million
FTE Position Change*	8.7 FTE	26.5 FTE	26.5 FTE
Effective Date: August 7, 2013, if the General Assembly adjourns on May 8, 2013, as scheduled, and no referendum petition is filed. Tax changes are effective beginning tax year 2014, subject to a trigger on future increases in the LCS or OSPB March revenue forecast, whichever is lower.			
Appropriation Summary for FY 2013-2014: See State Appropriations Section.*			
Local Government Impact: None.			

**This fiscal impact is conditional, predicated on the trigger contained within the bill having been met for tax year 2014. If the trigger is instead met in a future tax year, the fiscal impact would be shifted forward in time accordingly.*

Summary of Legislation

As amended by L.005, this bill makes the refundable Colorado earned income tax credit, currently a TABOR refund mechanism, permanent, and creates a refundable Colorado child tax credit. Table 1 compares Colorado state income tax credits under current law to those under Senate Bill 13- 001. More information about these credits and how they relate to their federal tax credit counterparts is contained within the background section.

The effective date of the bill is subject to a trigger on a future increase of at least $100 million in either the Legislative Council Staff (LCS) or Office of State Planning and Budgeting (OSPB) General Fund revenue forecast above the applicable March forecast, whichever March forecast is lower for the upcoming budget year. If the revenue forecast used for the trigger does not increase by at least $100 million within one year, the trigger resets for the following tax year. Once the trigger is met, the bill becomes permanently effective.

For example, the March 2013 OSPB General Fund revenue forecast is lower than the LCS forecast for FY 2013-14, the upcoming budget year. Therefore, if the OSPB forecast increases by at least $100 million in any of the four quarterly forecasts released between June 2013 and March 2014, the bill will become effective for tax year 2014. If this does not happen, the trigger will reset to whichever agency's March 2014 forecast for FY 2014-15 is lower, and the bill could not become effective until tax year 2015. This process will continue until the trigger is met.

Table 1. Colorado State Income Tax Credits Available Under SB13-001 (L.005)

Colorado Income Tax Credits	Treatment for Income Tax Credits: Current Law	Treatment for Income Tax Credits: Senate Bill 13-001 (L.005) *Effective Date Subject to A Trigger*
Colorado Child Tax Credit	Federal credit available. State credit not available.	Refundable state income tax credit equal to a percentage of the actual federal child tax credit claimed under Section 24 of the Internal Revenue Code. Children age 5 and under qualify. As a tax filer's income increases, the amount of the credit decreases. The credit is capped for single filers with federal adjusted gross income (AGI) of $75,000, and married filers with $85,000 of AGI.
Colorado Earned Income Tax Credit (EITC)	Refundable state income tax credit equal to 10% of federal EITC claimed. ***Available only during years for which the state has a TABOR surplus.***	Permanent refundable state income tax credit equal to 7% of the federal EITC claimed in the first year, 8.5% in the second year, and 10% in the third and subsequent years.

Background

The following provides historical and background information on the state and federal child and earned income tax credits and the changes under SB13-001, as amended by L.005. The federal credits are described because state credits are a percentage of their federal counterpart.

Colorado child tax credit. There is no state credit under current law. However, the state had previously extended a refundable child tax credit equal to $300 per child age 5 and under during years when the state had a sufficiently large TABOR surplus. Last available in 2000 and 2001, the credit was used as a mechanism to refund the TABOR surplus until it was repealed in 2010. Taxpayers claimed $30.5 million in FY 2000-01 and $37.4 million in FY 2001-02.

Federal credit. Under Section 24 of the Internal Revenue Code (IRC), the federal government allows a nonrefundable credit equal to $1,000 per qualifying child age 16 and under. The credit is phased-out for taxpayers with a federal adjusted gross income (AGI) over $75,000 for single filers and $110,000 for joint filers. An additional child tax credit is available and allows a portion of the child tax credit to be refundable for certain taxpayers who get less than the full amount of the child tax credit.

SB13-001 creates a refundable credit equal to a percentage of the federal credits claimed under Section 24 of the IRC. It includes a percentage of both the federal nonrefundable child tax credit and refundable additional child tax credits claimed. The credit is capped for single filers who have $75,000 in federal AGI and joint filers who have $85,000 in federal AGI. Thus, the credit is not available to taxpayers who have incomes above these thresholds.

Taxpayers filing single returns can qualify for a state income tax credit equal to:

- 30 percent of the federal credit claimed whenever federal AGI is below $25,001;
- 15 percent of the federal credit claimed whenever federal AGI is between $25,001 and $50,000; and
- 5 percent of the federal credit claimed whenever federal AGI is between $50,001 and $75,000.

Two taxpayers filing a joint return can qualify for a state income tax credit equal to:

- 30 percent of the federal credit claimed whenever federal AGI is below $35,001;
- 15 percent of the federal credit claimed whenever federal AGI is between $35,001 and $60,000; and
- 5 percent of the federal credit claimed whenever federal AGI is between $60,001 and $85,000.

Earned Income Tax Credit (EITC). The EITC is extended to low- and middle-income taxpayers who have earned income working for another person or from operating a business or farm.

The Colorado EITC is refundable and is equal to 10 percent of the federal EITC. One of three mechanisms in current law used to refund the TABOR surplus, the Colorado credit is only available during years when there is a TABOR surplus large enough to fund it. The Colorado EITC was last used to refund the FY 1998-99, FY 1999-00, and FY 2000-01 TABOR surpluses. In FY 2001-02, 210,942 taxpayers received an average EITC of $159, for a total General Fund tax refund of $32.9 million.

Federal credit. The federal EITC is refundable and varies depending on whether a taxpayer is single or married and the number of children in the home. For example, for tax year 2012, the maximum credit is $5,891 for households with three or more qualifying children and $475 for households with no qualifying children. Taxpayers must have an AGI less than a certain amount; for a taxpayer with three or more qualifying children that amount is $45,060 in 2012.

SB13-001 converts the Colorado EITC from a TABOR refund mechanism into a permanent refundable tax credit, making it available each year. However, the permanent tax credit would be equal to 7 percent of the federal EITC in the first year of implementation, 8.5 percent in the second year, and 10 percent in the third and later years of implementation.

State Revenue

General Fund revenue will be reduced $40.1 million in FY 2013-14, $88.0 million in FY 2014-15, and $104.1 million in FY 2015-16, conditional on the trigger in the bill being met for tax year 2014. If the trigger is not met until a future tax year, these revenue impacts will be shifted forward in time accordingly. The revenue impact for each credit is shown in Table 2 and described below.

Table 2. General Fund Revenue Impacts - SB13-001 as amended by L.005*
Millions of Dollars

	General Fund Revenue Impact		
Colorado Income Tax Credits	**FY 2013-14**	**FY 2014-15**	**FY 2015-16**
Colorado Child Tax Credit	($11.4)	($23.0)	($23.3)
Colorado Earned Income Tax Credit (EITC)	($28.7)	($65.0)	($80.8)
Total*	**($40.1)**	**($88.0)**	**($104.1)**

Totals may not sum due to rounding. FY 2013-14 represents a half-year impact.
**These estimates assume the trigger is met for tax year 2014.*

Child tax credit: General Fund revenue reduction of $11.4 million in FY 2013-14 and $23.0 million in FY 2014-15. This bill establishes a child tax credit equal to a percentage of the federal child tax credit claimed. Based on population estimates from the Office of the State Demographer and federal child tax credits claimed in 2010, an estimated 185,587 returns will be filed for children age 5 and under who will qualify for the state credit in tax year 2014. Of these returns, about 3,300, or 1.8 percent, are estimated to have claimed the federal additional child tax credit.

Earned income tax credit: General Fund revenue reduction of $28.7 million in FY 2013-14 and $65.0 million in FY 2014-15. This bill establishes a permanent Colorado EITC. Revenue estimates for the earned income tax credit are based on a history of federal earned income tax credits claimed by Colorado taxpayers and expectations for growth in the eligible population and the average earned income tax credit. Over a period of three years, based on an annual population of about 393,000 returns, the average EITC claimed will be about $186.

State Expenditures

Department of Revenue - General Fund expenditures will increase by $661,181 and 8.7 FTE in FY 2013-14 and $1,676,515 and 26.5 FTE in FY 2014-15. Table 3 shows General Fund expenditures for the Department of Revenue required to implement SB13-001.

Income Tax and Audit Sections. The income tax and audit sections will require $230,078 and 5.0 FTE in FY 2013-14 and $1,018,577 and 22.3 FTE in FY 2014-15 for auditing and verification costs. Based on the experience of the Internal Revenue Service, federal refundable tax credits have a higher rate of fraud and carry high auditing requirements.

Based on IRS statistics of income data for 2009 and American Community Survey data, approximately 441,212 households will be eligible for one or both of the credits in tax year 2014. In total, the income tax division is expected to review 10 percent of this amount, or 44,121 returns before authorizing the credits. In addition, the department is assumed to audit 25.5 percent of returns containing the earned income tax credit later in the year.

Table 3. Department of Revenue General Fund Expenditures Under SB13-001 (L.005)

Cost Components	**FY 2013-14**	**FY 2014-15**
Personal Services - Income Tax and Auditing Services	$ 230,078	$1,018,577
FTE	5.0	22.3
Personal Services - Call Center	$158,760	$180,213
FTE	3.7	4.2
Operating Expenses and Capital Outlay	$48,521	$108,421
Employee Insurance (Health, Life, Dental, and Short-Term Disability)*	$91,187	$276,397
Supplemental Employee Retirement Payments*	$26,635	$92,907
Programming Costs	$106,000	
TOTAL	**$661,181**	**$1,676,515**

* *Pursuant to a Joint Budget Committee policy, employee insurance and supplemental employee retirement payment costs are only appropriated within this bill rather than in the Long Bill or a supplemental appropriations bill when this bill requires more than 20 FTE.*

Call Center. The call center will require $158,760 and 3.7 FTE in FY 2013-14 and $180,213 and 4.2 FTE in FY 2014-15. It is expected that the Taxpayer Services Call Center will need to respond to about 44,121 additional calls related to the tax credits in Senate Bill 13-001 each year. This represents 10 percent of the 441,212 tax returns expected to contain one or both of the credits in the bill during tax year 2014, should the trigger make these credits available to taxpayers.

Programming costs. The department will incur one-time programing costs of $106,000 in FY 2013-14 to modify the GenTax system. GenTax is the department's new tax accounting program. Maintenance and updating are performed by contracts with the FAST Corporation and estimated at $200 per hour.

State Appropriations

Department of Revenue. The Department of Revenue will require a General Fund appropriation of $661,181 and 8.7 FTE in FY 2013-14.

Departments Contacted

Revenue Legislative Council Staff