

Colorado Legislative Council Staff Fiscal Note
STATE and LOCAL
FISCAL REVISED IMPACT

(replaces fiscal note dated February 2, 2010)

Drafting Number: LLS 10-0738
Prime Sponsor(s): Rep. Pommer
 Sen. Heath

Date: February 5, 2010
Bill Status: Senate Second Reading
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TITLE: CONCERNING THE STATE SALES AND USE TAX OF STANDARDIZED SOFTWARE, AND MAKING AN APPROPRIATION THEREFOR.

Fiscal Impact Summary	FY 2009-2010	FY 2010-2011	FY 2011-2012
State Revenue General Fund	\$4.6 million	\$23.7 million	\$24.1 million
State Expenditures General Fund	\$95,892*		
FTE Position Change	0.9 FTE		
Effective Date: Upon signature of the Governor, or upon becoming law without his signature. Effective for sales occurring on or after March 1, 2010.			
Appropriation Summary for FY 2010-2011: See the State Appropriations Section.			
Local Government Impact: See the Local Government Impact Section.			

* No separate appropriation for \$1,570 of these funds is required because of ongoing appropriations to the Department of Revenue for computer programming provided in the Long Bill for new legislation.

Summary of Legislation

As amended by the finance and appropriations committees of the Senate, this bill repeals the Department of Revenue regulation on taxable computer software. The regulation defines as tangible personal property, and therefore subjects to the sales and use tax, only pre-packaged software purchased in tangible form by a customer who also receives a license agreement. Examples of software defined as tangible personal property and therefore subject to sales and use tax as a result of this bill include:

- standardized software downloaded from the internet to the customer's computer or other electronic device;
- standardized software that is manually installed on a consumer's computer or electronic device by a vendor's representative.

The department is required to account for the revenue attributable to this bill, and to the extent information is available, make quarterly reports to the legislature about the revenue gain. The bill directs that at least 40 percent of the revenue estimated to have been collected as a result of this bill be spent on preschool through twelfth-grade education and directs that none of it be used to fund additional state FTE.

The bill allows the department to promulgate rules for apportioning tax liability when computer software is purchased for use in more than one state.

State Revenue

State General Fund revenue will increase \$4.6 million in FY 2009-10, \$23.7 million in FY 2010-11, and \$24.1 million in FY 2011-12. The revenue estimate for FY 2009-10 represents a partial-year impact. The revenue impact grows at a slower rate than expectations for growth in computer software sales in FY 2011-12 because, under current law, vendors will begin retaining 3.33 percent of the taxes they collect starting July 1, 2011.

Private expenditures on computer software in Colorado are estimated to be \$1.38 billion in 2010. About 60 percent of these expenditures are assumed to be affected by this bill; this assumption is based on figures from the software industry on the percentage of worldwide software sales related to the bill. Colorado expenditures were estimated using data from the Bureau of Economic Analysis on U.S. private prepackaged software sales. Colorado's share of U.S. expenditures is assumed to be the same as Colorado's share of personal income.

The inclusion of all standardized software in the definition of tangible personal property qualifies all manufacturers of standardized software for the sales tax exemption on equipment used in manufacturing. Thus, hardware and software used to develop software is assumed to be exempt from the state sales tax. Colorado software firms' expenditures on hardware and software are estimated to total \$35.8 million in 2010 based on data from the U.S. Census Service Annual Survey of 2008. Colorado's share of expenditures is assumed to equal its share of gross domestic product in the computer and electronic product manufacturing sector. Approximately 75 percent of these expenditures are assumed to be eligible for the exemption. Revenue estimates were reduced \$156,000 in FY 2009-10, \$796,000 in FY 2010-11, and \$808,000 in FY 2011-12 to account for this exemption.

State Expenditures

Department of Revenue: At least \$95,892 and 0.9 FTE in FY 2009-10. The Department of Revenue will incur one-time expenses in FY 2009-10 to notify vendors of the change and anticipates personnel costs to answer questions from vendors. The department will also incur additional General Fund information technology costs to adjust the state's computer systems. No appropriation for these information technology costs is necessary because of ongoing appropriations to the department for computer programming provided in the Long Bill for new legislation. Table 1 summarizes most of the costs incurred by the Department of Revenue.

Economies of scale. It should be noted that there are several pieces of legislation currently proposed that, if enacted, would affect sales and use tax account holders. If multiple bills are enacted, no separate appropriation may be required by this bill. The department will send one letter, two pages in length, to each sales and use tax account holder advising them of all enacted changes, rather than sending one notification for each legislative change.

Table 1. Expenditures Under HB10-1192	
Cost Components	FY 2009-2010
Information Technology Services	\$1,570
Personal Services	36,239
<i>FTE</i>	<i>0.9</i>
Operating Expenses	
Printing	5,999
Postage	52,084
TOTAL	\$95,892

Local Government Impact

This bill will result in an undetermined increase in revenue for local government entities. The inclusion of new forms of software in the definition of tangible personal property subject to taxation will affect the tax base of many local governments. The Regional Transportation District (RTD) has indicated it expects additional revenue of \$2.8 million each year as a result of this bill.

The reengrossed bill also specifies that at least 40 percent of the net revenue gain be appropriated to fund preschool through twelfth grade public education. This money must supplement and not supplant other funds used for this purpose. As a result, school districts will receive additional funding estimated at \$1.9 million in FY 2009-10 and \$9.5 million in FY 2010-11.

State Appropriations

For FY 2009-10, the bill requires a General Fund appropriation of \$94,322 and 0.9 FTE for the Department of Revenue. If multiple sales and use tax bills are enacted, no separate appropriation may be necessary for this bill.

Departments Contacted

Revenue
Law

Colorado Counties
RTD

Colorado Municipal League