Colorado Legislative Council Staff

SB16-001

FISCAL NOTE

FISCAL IMPACT: ☒ State ☐ Local ☐ Statutory Public Entity ☐ Conditional ☐ No Fiscal Impact

Drafting Number:	LLS 16-0669	**Date:**	January 20, 2016
Prime Sponsor(s):	Sen. Crowder	**Bill Status:**	Senate Finance
		Fiscal Analyst:	Kate Watkins (303-866-3446)

BILL TOPIC: UNLIMITED MILITARY RETIREMENT BENEFIT TAX DEDUCTION

Fiscal Impact Summary	FY 2016-2017	FY 2017-2018	FY 2018-2019
State Revenue	<u>**($11.6 million)**</u>	<u>**($23.9 million)**</u>	<u>**($25.4 million)**</u>
General Fund	($11.6 million)	($23.9 million)	($25.4 million)
State Expenditures		<u>**$109,377**</u>	<u>**$154,154**</u>
General Fund		$91,911	$122,252
Centrally Appropriated Costs		$17,466	$31,902
TABOR Impact	($11.6 million)	($23.9 million)	($25.4 million)
FTE Position Change		1.5	2.7
Appropriation Required: None.			
Future Year Impacts: Ongoing state revenue and expenditure impacts.			

Summary of Legislation

Under current law, qualifying taxpayers ages 55 to 64 may deduct up to $20,000 in retirement benefits from their taxable income each year and qualifying taxpayers ages 65 and older may deduct up to $24,000 each year. This bill eliminates these limitations for military retirement income, allowing taxpayers to deduct the entire amount of their military retirement income from state taxable income beginning in tax year 2017.

State Revenue

This bill is estimated to **reduce General Fund revenue by $11.6 million in FY 2016-17 (half-year impact), $23.9 million in FY 2017-18, and $25.4 million in FY 2018-19.** In future fiscal years, the revenue impact is expected to grow with the military retirement population and cost-of-living adjustments to military retirement benefits.

Assumptions. Data from the Department of Defense Office of the Actuary indicate that in federal fiscal year 2014, 45,816 retires in Colorado claimed $118.7 million monthly in military retirement benefits. This population excludes retirees who are disabled whose benefits are assumed to be excluded from federal taxable income. The 20,917 retirees over age 65 averaged an annual retirement income of $32,253. Those under 65 averaged $31,100 in annual retirement income, including an estimated 12,183 retirees ages 55 to 64 and 11,200 retirees under age 55.

These population and average payment amounts were grown by expectations for population and cost-of-living adjustments to arrive at estimates for tax year 2017 and beyond. The deduction under current law was then subtracted from the average retirement income amount for the above stated age groups to determine the difference between deductions claimed under current law and Senate Bill 16-001. Table 1 compares the estimated 2017 income tax liability reduction for taxpayers who claim the maximum deduction under current law and the projected average deduction under Senate Bill 16-001.

Table 1. Estimated Tax Year 2017 Income Tax Savings
(Calculated as the deduction amount multiplied by the state income tax rate of 4.63%)

Taxpayer Age	Under Current Law *(Maximum Deduction)*	Under SB 16-001 *(Average Deduction)*	Average Savings* under SB16-001
Below 55	$0	$31,152 × 4.63% = $1,442	$1,442
55 to 64	$20,000 × 4.63% = $926		516
65 and Over	$24,000 × 4.63% = $1,111	$32,801 × 4.63% = $1,519	408

**Assumes that the taxpayer has a large enough tax liability to receive additional savings.*

The estimated average taxpayer savings was then multiplied by the projected eligible population in each age group to arrive at a projection of the revenue impact of this bill. Not all qualifying taxpayers will have a Colorado income tax liability large enough to experience savings from this bill because many taxpayers claim other tax deductions and credits that reduce the taxes they owe. To account for this consideration, the projected revenue impact was reduced by 28.1 percent, an adjustment based on a weighted average of the tax liability and share of taxpayers ages 65 and older using data from the 2012 Colorado statistics of income.

TABOR Impact

This bill reduces state revenue from the General Fund, which will reduce the amount of money required to be refunded under TABOR. TABOR refunds are paid out of the General Fund. Table 2 shows the projected impact on the mechanisms used to refund the TABOR surplus under current law. This bill is expected to reduce the TABOR surplus by $11.6 million in FY 2016-17 and $23.9 million in FY 2017-18, reducing the amount of revenue refunded through the Six Tier Sales Tax Refund by these amounts.

Table 2. Impact of SB 16-001 on Current Refund Mechanisms *(Millions of Dollars)*		
	FY 2016-17 Surplus FY 2017-18 Refund Tax Year 2017	FY 2017-18 Surplus FY 2018-19 Refund Tax Year 2018
Current Law		
Revenue above the TABOR limit	$191.6 million	$384.2 million
Income Tax Rate Reduction	0	232.9 million
Sales Tax Refund	191.6 million	151.3 million
SB 16-001		
Revenue above the TABOR limit	180.0 million	360.3 million
Income Tax Rate Reduction	0	232.9 million
Sales Tax Refund	180.0 million	127.4 million
Change from Current Law		
Revenue above the TABOR limit	(11.6 million)	(23.9 million)
Income Tax Rate Reduction	0	0
Sales Tax Refund	(11,6 million)	(23.9 million)
Total Change from Current Law	**($11.6 million)**	**($23.9 million)**

Source: Legislative Council Staff December 2015 forecast.

State Expenditures

This bill will increase General Fund expenditures for the **Department of Revenue by $109,337 and 1.5 FTE in FY 2017-18 and $154,154 and 2.7 FTE in FY 2018-19**. Costs include personal services, operating expenses, form change and programming costs, as summarized in Table 3.

Table 3. Expenditures Under SB 16-001			
Cost Components	**FY 2016-17**	**FY 2017-18**	**FY 2018-19**
Personal Services		$63,880	$114,984
FTE		1.5	2.7
Operating Expenses and Capital Outlay Costs		10,831	7,268
Form Change and Programming		17,200	
Centrally Appropriated Costs*		17,466	31,902
TOTAL		**$109,377**	**$154,154**

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

Taxpayer Service Division costs. The deduction under this bill requires minimal audit work to verify retirement income as this amount is reported on federal income tax returns. Fifteen percent of the claims filed for the deduction in tax years 2017 and 2018 are expected to be reviewed by a Tax Examiner I. This will require 1.3 FTE in FY 2017-18 and 2.5 FTE in FY 2018-19.

Call Center. New tax expenditures tend to result in higher call center volumes. Ten percent of the qualifying population is assumed to require call center services for tax year 2017 and 5 percent for tax year 2018 returns, requiring 0.2 FTE in FY 2017-18 and FY 2018-19.

Form change and programming costs. This bill requires programming and reconfiguring of the document imaging system to insert an additional line to capture the deduction value on individual income tax form 104CR. This will require one-time programming costs of $1,200 in FY 2017-18, which will be reappropriated from the Department of Revenue to the Department of Personnel and Administration. An additional $16,000 (80 hours of contract work at $200 per hour) in one-time programming costs is required to modify the GenTax tax processing software system.

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. The centrally appropriated costs subject to this policy are estimated in the fiscal note for informational purposes and summarized in Table 4.

Table 4. Centrally Appropriated Costs Under SB 16-001

Cost Components	FY 2017-18	FY 2018-19
Employee Insurance (Health, Life, Dental, and Short-term Disability)	$12,000	$21,599
Supplemental Employee Retirement Payments	5,466	10,303
TOTAL	**$17,466**	**$31,902**

Effective Date

The bill takes effect August 10, 2016, if the General Assembly adjourns on May 11, 2016, as scheduled, and no referendum petition is filed.

State and Local Government Contacts

Revenue   Military and Veterans Affairs