HB 21-1312

Legislative Council Staff

Nonpartisan Services for Colorado's Legislature

Fiscal Note

Drafting Number:	LLS 21-0502	**Date:**	May 13, 2021
Prime Sponsors:	Rep. Weissman; Sirota Sen. Hansen; Moreno	**Bill Status:**	House Finance
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Bill Topic: **SEVERANCE TAX CREDIT FOR PROPERTY TAXES**

Summary of Fiscal Impact:

☒ State Revenue
☒ State Expenditure
☐ State Transfer
☒ TABOR Refund
☒ Local Government
☐ Statutory Public Entity

The bill makes various changes to the insurance premium, property, sales and use, and severance taxes. The bill is expected to increase state revenue and expenditures beginning in FY 2021-22.

Appropriation Summary: For FY 2021-22, the bill requires an appropriation of $274,142 to the Department of Revenue and $138,500 to the Division of Property Taxation. See the State Appropriations section.

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

Table 1
State Fiscal Impacts Under HB 21-1312

		Budget Year FY 2021-22	Out Year FY 2022-23
Revenue	General Fund	$132.7 million – $134.8 million	$150.1 million – $153.9 million
	Just Transition Cash Fund	$0.2 million	$0.7 million
	Total	**$132.9 million – $135.0 million**	**$150.8 million – $154.6 million**
Expenditures	General Fund	$19.3 million	$19.1 million
Transfers		-	-
TABOR Refund	General Fund	-	**$122.2 million – $126.0 million**

Summary of Legislation

The bill makes changes to the state insurance premium tax, sales and use tax, and the severance tax, and makes changes to the administration of property tax. These changes are described in greater detail below.

Insurance Premium Tax

The bill makes two changes to the insurance premium tax. Under current law, insurance premiums are taxed at a rate of two percent, except that insurance companies with a regional home office in Colorado are taxed at a rate of one percent. To qualify for the regional home office designation, a company must either substantially perform particular insurance company functions in Colorado, or maintain significant direct insurance operations in the state. Under this bill, insurance companies will also have to maintain at least 2.5 percent of their domestic workforce in Colorado to qualify for regional home office designation and the associated lower tax rate.

Additionally, under current law, the insurance premium tax does not apply to premiums from policies or contracts issued in connection with an annuity plan. Under this bill, premiums connected to annuity plans will only be exempt from the insurance premium tax if the annuity plan is purchased in connection with a qualified retirement plan, a Roth 401(k), or an individual retirement account.

Property Tax

Business personal property tax exemption. Under current law, businesses are not required to pay tax on their personal property, if their personal property included on a single tax schedule is worth less than a certain amount. For tax years 2021 and 2022, the exemption threshold is $7,900 under current law. The bill increases the threshold amount to $50,000, adjusted every two years for inflation thereafter.

The state is required to reimburse local governments for their lost revenue as a result of the increased exemption. For tax year 2021, each county is required to calculate and report the amount of revenue lost. Using the statewide rate of change in personal property valuation prepared by the property tax administrator, each county is required to produce an annual estimate of the amount of lost property tax revenue for each of its taxing jurisdictions based on the amounts of lost revenue reported for 2021. Subject to review by the property tax administrator, these amounts are reimbursed to local governments each year from the state treasury via each county treasurer.

Property tax administration. The bill clarifies that a property's actual value reflects the value of the "fee simple estate," a term which the bill defines, and the property's highest and best use. For personal property, the bill clarifies that the actual value is based on the property's value in use.

Sales and Use Tax

Taxation of digital goods and services. The bill codified existing practice by adding digital goods to the definition of tangible personal property for state sales and use taxation. The definition includes property such as videos, music, and electronic books that are delivered or stored digitally via compact disc, electronic download, or internet streaming.

In addition, the bill adds mainframe computer access, photocopying, and packing and crating to property and services taxed.

Vendor fee changes. The bill also eliminates the vendor fee retained by retailers from sales and use tax collections for those with taxable sales greater than $1 million each month beginning January 2022. The current vendor fee is equal to 4 percent of state sales and use tax collections, up to $1,000 per account per filing period.

Severance Tax

Oil and gas – netback deduction. Under current law, the severance tax is applied to the net amount realized by the taxpayer for the sale of oil or gas. Taxpayers are currently able to deduct from the net amount *any* transportation, manufacturing, and processing costs borne by the taxpayer. The bill would restrict the deduction to transportation, manufacturing, and processing costs that are direct costs actually paid by the taxpayer. The bill also grants the Department of Revenue (DOR) rulemaking authority regarding the net amount calculations.

Coal – tonnage exemption and tax credits. Under current law, the first 300,000 tons of coal produced each quarter are exempt from the severance tax on coal. Additionally, there is a 50 percent tax credit for coal produced from both underground mines and lignitic coal. Between 2022 and 2026, the bill phases out all three of these tax expenditures as shown in Table 2 below. Any increased severance tax revenue resulting from these changes is to be deposited into the Just Transitions Cash Fund.

Table 2
Allowable Coal Tonnage Exemption and Tax Credits Under HB 21-1312

Tax Year	Production Exemption	Underground Mine Credit*	Lignitic Coal Credit*
2021	Up to 300,000 tons	50%	50%
2022	Up to 240,000 tons	40%	40%
2023	Up to 180,000 tons	30%	30%
2024	Up to 120,000 tons	20%	20%
2025	Up to 60,000 tons	10%	10%
2026	0	0%	0%

*Allowable credit as a share of the severance tax imposed.

Background

Business personal property tax. Property taxes may apply to personal property in addition to real property. Business personal property means movable items owned by a business, including for example machinery, computers, and furniture. Real property includes land, structures, and other improvements.

Vendor fee. Retailers are required to collect and remit sales and use tax and are allowed to retain a fee, which has changed over time as shown in Table 3. Under current law, vendors may retain four percent of collections, up to $1,000 per month, to cover their expenses for collecting and remitting sales and use tax.

Table 3
Colorado Vendor Fee History

Dates	Vendor Fee
July 1, 1935 to June 30, 1965	5.00 percent
July 1, 1965 to June 30, 2003	3.33 percent
July 1, 2003 to June 30, 2005	2.33 percent
July 1, 2005 to February 28, 2009	3.33 percent
March 1, 2009 to June 30, 2009	1.35 percent
July 1, 2009 to June 30, 2011	0 percent
July 1, 2011 to June 30, 2014	2.22 percent
July 1, 2014 to December 31, 2019	3.33 percent
January 1, 2020 to current	4.00 percent[1]

[1] *Subject to a $1,000 cap for each retailer per month.*

Assumptions

Economic forecast. All revenue estimates assume future economic activity consistent with the March 2021 Legislative Council Staff forecast update.

State Revenue

The bill is expected to increase General Fund Revenue by between $132.9 million and $135.0 million in FY 2021-22, and by between $150.8 million and $154.6 million in FY 2022-23 and subsequent years. Revenue impacts are present in Table 4 and discussed below. The bill increases state revenue from the insurance premium, sales and use, and severance taxes, all of which are subject to TABOR.

Table 4
Revenue Under HB 21-1312

	FY 2021-22	FY 2022-23
Insurance Premium Tax		
Regional Home Office Modification	$60.5 million	$64.7 million
Annuities Tax Treatment Modification	$55.3 million	$59.2 million
Sales and Use Tax		
Mainframe computer access, photocopying, and packing and crating	$9.5 million – $11.6 million	$10.7 million – $14.5 million
Vendor fee	$7.4 million	$15.6 million
Severance Tax		
Coal Tonnage Exemption	$0.1 million	$0.4 million
Underground Mine Tax Credit	$0.08 million	$0.2 million
Total	**$132.9 million – $135.0 million**	**$150.8 million – $154.6 million**

Insurance Premium Tax

Regional home office modification. This provision is expected to increase state revenue by approximately $60.5 million in FY 2021-22 and by $64.7 million in FY 2022-23 and in subsequent years. In 2019 (the most recent year for which data are available), approximately 80 insurance companies qualified for the regional home office designation, and the regional home office tax expenditure reduced tax revenue by approximately $102.1 million. Of those 80 companies, about half qualified for the designation by maintaining significant direct insurance operations in Colorado. The fiscal note assumes that these companies will continue to qualify for the regional home office designation under the bill. As such, the additional criteria imposed by this bill is expected to reduce the value of this tax expenditure by about 50 percent. Under this bill, tax revenue would have been about $51.1 million higher in 2019. To arrive at the estimates for FY 2021-22 and FY 2022-23, the estimate for 2019 was increased by 7 percent per year, the average insurance premium growth rate between 2015 and 2019. Estimates may be higher or lower depending on actual growth rates.

Annuities tax treatment modification. This provision is expected to increase state revenue by approximately $55.3 million in FY 2021-22, and by $59.2 million in FY 2022-23 and subsequent years. As of 2019, total annuities premiums, less those paid to fraternal organizations, amounted to $5.6 billion. Based on estimates from the Life Office Management Association, an insurance-industry trade association, approximately 42 percent of annuities premiums are not connected to retirement plans, or about $2.3 billion in premiums. Based on these figures, in 2019 this provision would have increased insurance premium tax revenue by $46.7 million. To arrive at the estimates for FY 2021-22 and FY 2022-23, the estimate for 2019 was increased by 7 percent per year, the average insurance premium growth rate between 2015 and 2019. Estimates may be higher or lower depending on actual growth rates.

Sales and Use Tax

Sales and use tax mainframe computer access, photocopying, and packing and crating. This provision is expected to increase state revenue by between $9.5 million and $11.6 million in FY 2021-22 and between $10.7 million and $14.5 million in FY 2022-23, with ongoing revenue growth in subsequent years depending on industry growth rates and product profiles. A range of revenue is presented to account for faster than expected industry growth, as fast as 26 percent per year based on private reports quantifying the cloud-storage market. About 93 percent to 95 percent of the revenue increase is attributed to mainframe computer access, related to cloud-based data storage services. Sales and use tax attributable to packing and crating is assumed to comprise the remaining impact of the bill on revenue. While most taxable sales consider the cost of shipping materials in the purchase price of tangible personal property, the bill is assumed to expand taxable purchases to companies involved in preparing goods for shipping. The inclusion of photocopying in the bill is assumed to result in a minimal revenue increase. The market for photocopying services likely comprises a shrinking market with the proliferation of home and office printers and electronic documents.

The revenue impact for mainframe computer access is based on the estimated share of Colorado's data processing, internet publishing, and other information services industry based on data from the U.S. Bureau of Economic Analysis. Estimated sales were grown based on the annual rate recorded for the data processing, internet publishing, and other information services industry over the past three years. The revenue impact of packing and crating assumes taxable sales of between $23.4 million and $23.9 million each year based on the number of establishments in the state and data from the 2017 Economic Census, adjusted for inflation.

Eliminate vendor fee for large retailers. This provision is expected to increase state revenue by $7.4 million in FY 2021-22 (half-year impact) and $15.6 million in FY 2022-23, with similar revenue impacts in subsequent years Revenue derived from the bill is expected to increase in future years with changes in sales tax revenue. In 2020, approximately 165,540 sales and use tax accounts retained a total of $58.6 million. The vendor fee will be eliminated for an estimated 1,215 accounts under the bill. These retailers retained an estimated $13.7 million of the total vendor fee. This revenue estimate assumes a similar distribution of sales by net taxable category and a similar number of accounts as exists under current law.

Severance Tax

Modified netback deduction. This provision will increase severance tax revenue by an indeterminate amount beginning in FY 2021-22. However, due to a lack of data regarding this provision this amount is not estimated.

Coal tonnage exemption. Phasing out the coal tonnage exemption is expected to increase severance tax revenue by $143,000 in FY 2021-22 (half-year impact), by $448,000 in FY 2022-23, and $790,000 in FY 2023-24. This estimate is based on the September 2020 Office of the State Auditor's report (http://leg.colorado.gov/sites/default/files/2020-te30_coal_severance_tax_expenditures.pdf). Lignitic coal has not been produced in Colorado for several years, and is unlikely to be mined in the state in the future. In 2020, or the six producing coal mines in the state, two were surface mines accounting for 35 percent of the production and four were underground mines accounting for 65 percent of the production. Historical estimates of the revenue impact for the exemption have been adjusted downward to reflect actual and estimated future decreases in coal production in Colorado.

Underground mine tax credit. Phasing out the tax credit for underground coal mines is expected to increase severance tax revenue by $78,000 in FY 2021-22 (half-year impact), by $246,000 in FY 2022-23, and by $434,000 in FY 2023-24. This estimate is based on the September 2020 Office of the State Auditor's report. Historical estimates for the revenue impact of the credit have been adjusted downward to reflect actual and estimated future decreases in coal production in Colorado.

Income Tax

Business personal property tax credit. Current law allows an income tax credit for property tax paid on up to $18,000 in business personal property. The expanded business personal property tax exemption will reduce claims of the income tax credit, thereby increasing state revenue from income taxes. Because property taxes are paid in arrears, income tax revenue will first increase in tax year 2022, when property taxes paid for the 2021 property tax year will decrease. Based on data for claims of the credit for tax year 2019, the revenue increase from reduced credit claims is expected to be less than $100,000 per year.

State Expenditures

The bill is expected to increase General Fund expenditures by $19,331,339 and 1.3 FTE in FY 2021-22, and $19,070,239 and 1.0 FTE in FY 2022-23, with similar impacts in subsequent years. Expenditures are summarized in Table 5 and described below.

Table 5
Expenditures Under HB 21-1312

Cost Components	FY 2021-22	FY 2022-23
Department of the Treasury		
Property Tax Exemption Reimbursements	$18,900,000	$19,000,000
Treasury Subtotal	**$18,900,000**	**$19,000,000**
Department of Revenue		
Personal Services	$62,960	$54,003
Operating Expenses	$1,755	$1,350
Capital Outlay Costs	$6,200	-
GenTax Computer Programming	$166,050	-
Computer and User Acceptance Testing	$24,290	-
Sales and Use Tax System Computer Programming	$12,375	-
Tax Form Changes	$512	-
Centrally Appropriated Costs[1]	$18,696	$14,887
FTE – Personal Services	1.3 FTE	1.0 FTE
DOR Subtotal	**$292,839**	**$70,239**
Department of Local Affairs – Division of Property Taxation		
Computer Programming	$138,500	-
DOLA - PTD Subtotal	**$138,500**	**$0**
Total	**$19,331,339**	**$19,070,239**
Total FTE	**1.3 FTE**	**1.0 FTE**

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

Department of the Treasury. The bill requires reimbursements to local governments for the property tax loss associated with the expanded business personal property tax exemption. Reimbursements are estimated at $18.9 million in FY 2021-22 for the 2021 property tax year, and $19.0 million in FY 2022-23 for the 2022 property tax year. Estimates are based on prior year business personal property tax records, adjusted according to the December 2020 Legislative Council Staff forecast for assessed values.

School finance. Because the state is required to reimburse local governments for their lost property tax revenue, it is assumed that the bill has no impact on the local share of funding for school finance, and that no corresponding adjustment to the state share is required.

Department of Revenue. The bill is expected to increase expenditures for DOR by $292,839 and 1.3 FTE in FY 2021-22, and by $70,239 and 1.0 FTE in FY 2022-23 and subsequent years.

Beginning in FY 2021-22, DOR will require an additional 0.6 FTE analyst to assist with rulemaking, issuing general information letters, and making private letter rulings. This work is driven mainly by the changes to the sales and use tax and severance tax. Additionally, DOR will require an additional 0.7 FTE tax examiners in FY 2021-22 and 0.4 FTE tax examiners in FY 2022-23 and subsequent years to process increased sales and use tax returns.

Other costs for the department are related to programming the department's GenTax software and the Sales and Use Tax System software, software and related user acceptance testing, and tax form changes performed in the Department of Personnel and Administration using reappropriated DOR funds.

Department of Local Affairs – Division of Property Taxation. The bill will increase workload in the Division of Property Taxation (DPT) beginning in FY 2021-22, and require a one-time expenditure for computer programming in FY 2021-22. The bill's provisions requiring the DPT to calculate the percentage change in total value of business personal property and to review and approve the amounts reported by county treasurers will result in a workload increase for the DPT. This increased workload can be accomplished within existing appropriations.

Additionally, one-time expenditures of $138,500 are required to establish a new portal for county treasurers to submit their estimated tax reimbursement amounts. These funds will be reappropriated to the Office of Information and Technology who will design and build the new portal.

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 $18,696 in FY 2021-22 and $14,887 in FY 2022-23.

TABOR refunds. The bill increases state revenue subject to TABOR. On net, the bill is expected to increase state revenue subject to TABOR by the amounts shown in Table 6.

As shown, the bill is expected to result in a TABOR surplus of $122.2 million to $126.0 million in FY 2022-23. The surplus will be refunded in FY 2023-24 via property tax exemptions for seniors and disabled veterans, partially offsetting the amount of FY 2023-24 General Fund revenue that would otherwise be expended for this purpose. Actual refunds will depend on state revenue collected in FY 2022-23, which will depend on economic conditions and any other enacted policy changes.

Table 6
State TABOR Outlook Under HB 21-1312

	Budget Year FY 2021-22	Out Year FY 2022-23
Current Law TABOR Surplus or (Deficit)	($328.7 million)	($28.6 million)
Plus: Change in TABOR Revenue	$132.9 million – $135.0 million	$150.8 million – $154.6 million
TABOR Surplus or (Deficit) under HB 21-1311	**($195.8 million – $193.7 million)**	**$122.2 million – $126.0 million**

Source: March 2021 Legislative Council Staff forecast. A forecast of state revenue subject to TABOR is not available beyond FY 2022-23.

Local Government

Property tax. The expanded business personal property tax exemption in the bill is assumed not to affect local government revenue, as lost property tax revenue is offset by a state reimbursement. However, the bill requires that revenue losses be calculated as if business personal property valuations would increase at the same rate in all areas of the state. Local governments where personal property valuations would increase more quickly than the rest of the state will experience a marginal revenue decrease, while local governments where personal property valuations would increase less quickly than the rest of the state will experience a marginal revenue increase. The bill may decrease local government TABOR refund obligations for local governments where voters have exempted state government revenue distributions, but not property tax revenue, from the local TABOR limit.

The bill increases FY 2021-22 workload for county assessors to estimate the amount of lost property tax revenue. It decreases workload in future years when fewer assessments of personal property will be required.

The provisions of the bill that address property tax valuation codify current practice and are assumed to have no fiscal impact.

Sales and use tax. The provision extending sales taxable property and services to mainframe computer access will increase sales and use tax revenue for state-collected local governments and special districts that conform to the state tax base. This analysis does not estimate the pattern of consumer and business purchases for each area within the state.

Technical Note

The provision extending sales taxable property and services to mainframe computer access is assumed to apply to the purchase price of cloud-based data storage services only. However, the bill may be interpreted to extend to data storage infrastructure as a service or other cloud-computing or processing services. If mainframe computer access is interpreted to encompass a broader range of services and industries, the bill may increase General Fund revenue by a larger among than that included in this fiscal note.

Effective Date

The bill takes effect July 1, 2021.

State Appropriations

For FY 2021-22, the bill requires a General Fund appropriation of $274,142 to the Department of Revenue, with an allocation of 1.3 FTE. From this amount, $512 should be reappropriated to the Department of Personnel and Administration. In addition, the bill requires a General Fund appropriation of $138,500 to the Division of Property Taxation, which should be reappropriated to the Office of Information and Technology.

Expenditures for reimbursements to local governments for lost property tax revenue are assumed not to require an appropriation, consistent with the treatment of the senior and disabled veteran homestead exemptions in current budget documents.

State and Local Government Contacts

Corrections
Counties
County Assessors
County Clerks
Education
Information Technology
Local Affairs
Municipalities
Natural Resources
Office of Economic Development and International Trade
Office of State Planning and Budgeting
Personnel
Property Tax Division - Local Affairs
Regional Transportation District
Regulatory Agencies
Revenue
Special Districts