Office of the State Auditor

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MEMORANDUM

Date: November 13, 2018

To: Joint Budget Committee

From: Dianne E. Ray, State Auditor

Re: Tax Expenditures Evaluation Resource Needs

The purpose of this memo is to outline resource constraints that will make it difficult for the Office of the State Auditor (OSA) to complete evaluations of all of the State's tax expenditure provisions by September 2022, as required by Senate Bill 16-203, and provide potential options for addressing these constraints.

SENATE BILL 16-203 FISCAL NOTE AND APPROPRIATION

Under Senate Bill 16-203, the OSA was appropriated 3.2 additional staff to complete the required tax expenditure evaluations. This level of staffing was based on a review of similar evaluations that are conducted by the State of Washington through its Joint Legislative Audit Review Committee (JLARC). Washington has over 600 tax expenditure provisions, which JLARC must review on a 10 year cycle, with about 4.5 FTE assigned to the evaluations. The staffing appropriated to the OSA was calculated to be commensurate to the staffing levels for JLARC, taking into account that there are fewer tax expenditures in Colorado and a 5-year review period.

We have found that two key assumptions that we used in estimating our capacity for fiscal note purposes were not accurate. First, although our estimates accounted for a substantial portion of JLARC's evaluations taking less time, we assumed that JLARC was completing a substantive evaluation of each provision and that its staff were able to complete about 60 evaluations each year. However, after meeting with JLARC

staff and reviewing their process in detail, we learned that in practice, JLARC only completes substantive evaluations for about 15-20 tax expenditure provisions each year. They are able to complete the other required reviews by completing most of them as "expedited." Under Washington's statutes, JLARC can fulfill the required review for these expedited evaluations by simply republishing revenue impact estimates already prepared by Washington's Department of Revenue or information prepared by JLARC staff from prior year reviews, which requires minimal staff time. JLARC also classifies some expenditures as "critical to the tax structure," in which case they are not reviewed by staff. However, for the OSA's evaluations this approach would not comply with Senate Bill 16-203, which requires a substantive review of each expenditure provision.

Second, we based our staffing estimates on Colorado having 185 tax expenditure provisions. However, after completing our review of statute, we have identified 216 tax expenditures that will require review, about 17 percent more than originally estimated.

LONG-TERM RESOURCE NEEDS/OPTIONS

During the first year of conducting tax expenditure evaluations, the OSA completed 15 evaluations, leaving 201 remaining for completion by September 2022 to comply with statute. The OSA's tax expenditure team currently has 3.5 permanent assigned staff, and two full-time interns, for a total of 5.5 staff working on evaluations. Based on the time each evaluation took in 2018 and with current staffing levels, we estimate that we will be able to complete, on average, about 25 tax expenditure evaluations each year. However, to complete the remaining 201 tax expenditure evaluations in the next 4 years, as required by statute, the team would need to review about 50 expenditures each year. Although we are likely to see some continued improvement in process efficiencies, we do not expect to be able to complete 50 evaluations each year, given current statutory requirements for the evaluations. Therefore, we are requesting legislative approval for changes to one or more of the following variables to be able to comply with our statutory requirement: (1) Reduce the scope of some evaluations, (2) Extend the statutory timeline past 2022, and/or (3) Increase FTE. We discuss these options below.

REDUCE THE SCOPE OF SOME EVALUATIONS

We could meet our statutory deadlines by significantly reducing the scope of some of our evaluations, and treating them as "expedited evaluations." However, based on the requirements in Senate Bill 16-203, we do not believe that we currently have this discretion to the extent necessary to address our current resource constraints. Thus, for this option to be effective, we would need statutory changes to provide us with

additional discretion over the types of analyses to include in each evaluation based on our available resources (See APPENDIX A for a draft of potential statutory changes). EXHIBIT 1 provides the current statutory requirements, a description of our current minimum level of work necessary to address each requirement, and how that level of work would change for expedited evaluations, if allowed more discretion over the scope of our reviews. (See APPENDIX B for an example of what an expedited evaluation would look like.)

EXHIBIT 1. PROPOSED CHANGES TO SCOPE OF EVALUATIONS IF EXPEDITED REVIEWS ARE ALLOWED		
CURRENT STATUTORY EVALUATION REQUIREMENTS	CURRENT MINIMUM LEVEL OF REVIEW FOR EVALUATIONS	PROPOSED CHANGES FOR EXPEDITED EVALUATION LEVEL OF REVIEW
Outreach to intended beneficiaries or their representatives	Contact a small sample of beneficiaries or representatives that can easily be identified for interviews.	No change
Summary of the purpose, intent, or goal of the expenditure	Determine based on statute and a brief review of available legislative history.	No change
Summary of the beneficiaries	Determine based on what is provided in statute, beneficiary outreach, or easily inferable.	No change
Explanation of the performance measures used to determine the extent to which the tax expenditure is accomplishing its purpose, intent or goals	Create performance measures for all expenditures and perform enough analysis to answer them if possible.	Create no performance measures and just state that statute did not provide any. If statute includes a performance measure (which is rare), the evaluation will not be expedited.
A conclusion on whether the expenditure is meeting its purpose	Conclusion is based on our analysis of performance measures. If information is available, conduct analysis sufficient to conclude on whether it is meeting its purpose.	Based on data readily available from the Department of Revenue or other sources. Because we will not create performance measures and will likely pick expenditures with less available data for expedited reviews, the answer here will often be "could not determine based on available information."
An explanation of the economic impact that was intended	Explain the intended economic impact if inferable from statute and also attempt to, at a minimum, provide an estimated revenue impact to the State, if reasonably possible.	Explain the intended impact if inferable from statute. Conduct no analysis of that intended impact and only provide a revenue impact if Department of Revenue data is readily available.
Summary of other states with similar tax expenditures	Based on what we can pull from Lexis Nexis and a limited web-search.	No change
Summary of other expenditures or programs with a similar purpose	Based on the information we identify through a limited search.	No change
Data constraints	Report known data constraints that would impact the analysis.	No change

EXTEND STATUTORY DEADLINE

Based on our analysis, we would need to extend the statutory deadline 4 years (2026), to complete evaluations for the remaining 201 tax expenditures if no other changes are made. Under this scenario, we would need to complete an average of 25 evaluations each year, applying the current scope of review.

INCREASE FTE

Increasing our appropriated resources by 1.0 FTE would also help us to complete our evaluations faster. However, this option alone would only increase the number of evaluations we could complete each year, applying the current scope of review, by six. Under this scenario, we would still not be able to meet the current 2022 statutory deadline. We would need to extend the statutory deadline by 3 years (2025) to complete the remaining 201 evaluations.

OPTIONS FOR ADDRESSING RESOURCE NEEDS

EXHIBIT 2 shows the various options that are available to help us comply with our statutory requirements, applying the three variables discussed above. Under these options, we are assuming that we will conduct the minimum number of evaluations as expedited to allow us to meet the applicable deadline.

EXHIBIT 2. PROJECTED EVALUATIONS COMPLETED EACH REVIEW YEAR[1] UNDER POTENTIAL OPTIONS (WITH ESTIMATED NUMBER OF EXPEDITED REVIEWS IN PARENTHESES)

OPTIONS	ALLOW EXPEDITED?	FTE INCREASE[3]	2018 (ACTUAL)	2019	2020	2021	2022 (CURRENT DEADLINE)	2023	2024	2025	2026
# 1 (No changes)	No	0	15	24	26	27	27	27	27	27	16
#2	No	1	15	24	32	33	33	33	33	13	
#3[2]	Yes	0	15	30 (9)	33 (9)	34 (9)	34 (8)	35 (8)	35 (8)		
#4[2]	Yes	1	15	33 (12)	40 (12)	42 (11)	43 (11)	43 (11)			
#5[2]	Yes	0	15	37 (17)	40 (17)	41 (17)	41 (17)	42 (17)			
#6[2]	Yes	1	15	44 (24)	51 (24)	53 (24)	53 (24)				
#7[2]	Yes	0	15	48 (30)	50 (29)	51 (29)	52 (29)				

[1] The estimated schedules only include completing the initial 216 expenditure reviews identified by the OSA; they do not include any additional expenditures approved by the General Assembly that would need to be reviewed prior to 2022. Each review year begins on September 15 and ends on September 14 of the year indicated.
[2] Capacity assumes a 15.5 percent increase in efficiency from 2018 to 2021.
[3] Estimates assume staffing changes occur in July 2019.

APPENDIX A: Potential Statutory Changes (Bold)

39-21-305. Tax expenditure - state auditor evaluation

(1) (a) The state auditor shall evaluate the state's tax expenditures pursuant to the requirements in this section. In evaluating each tax expenditure, the state auditor shall consult with the intended beneficiaries or representatives of the intended beneficiaries of the tax expenditure. In addition, if the tax expenditure is intended to benefit a specific geographic region of the state, the state auditor shall consult with the intended beneficiaries in that specific geographic region of the state.

(b) **TO THE EXTENT IT CAN BE DETERMINED BY THE STATE AUDITOR USING AVAILABLE RESOURCES**, the state auditor's tax expenditure evaluation ~~must~~ **SHOULD** include the following:

(I) A summary description of the purpose, intent, or goal of the tax expenditure;

(II) The intended beneficiaries of the tax expenditure;

(III) Whether the tax expenditure is accomplishing its purpose, intent, or goal;

(IV) An explanation of the intended economic costs and benefits of the tax expenditure, with analyses to support the evaluation if they are available or reasonably possible;

(V) A comparison of the tax expenditure to other similar tax expenditures in other states;

(VI) Whether there are other tax expenditures, federal or state spending, or other government, nonprofit, commercial, volunteer, or philanthropic programs, to the extent the information is readily available, that have the same or similar purpose, intent, or goal as the tax expenditure, how those all are coordinated, and if coordination could be improved, or whether any redundancies can be eliminated;

(VII) If the evaluation of a particular tax expenditure's economic impact is made difficult because of data constraints, any suggestions for changes in administration or law that would facilitate such data collection; and

(VIII) An explanation of the performance measures used to determine the extent to which the tax expenditure is accomplishing its purpose, intent, or goal. The performance measures must be clear and relevant to the specific tax expenditure being evaluated, should be measurable and track actionable goals, and can be assessable and reportable over time. The state auditor shall consider the original legislative intent as well as subsequent developments in the state's economy, the national economy, and any changes in national, state, or local fiscal policies and conditions.

(c) To the extent it can be determined by the state auditor **USING AVAILABLE RESOURCES**, the tax expenditure evaluation should also include the following:

(I) The extent to which the tax expenditure is a cost-effective use of resources compared to other options for using the same resources to address the same purpose, intent, or goal;

(II) An analysis of the tax expenditure's effect on competition and on business and stakeholder needs;

(III) Whether there are any opportunities to improve the effectiveness of the tax expenditure in meeting its purpose, intent, or goal; and

(IV) An analysis of the effect of the state tax policies connected to local taxing jurisdictions on the overall purpose, intent, or goal of the tax expenditure.

(d) No later than September 15, 2017, the state auditor shall develop and publish a multi-year schedule that lists all tax expenditures in law as of July 1, 2017, and indicates the year when the evaluation report will be published for each tax expenditure. In developing the multi-year schedule the state auditor shall endeavor to review the oldest tax expenditures first and shall endeavor to review a tax expenditure with a statutory repeal date so that the evaluation report for such tax expenditure is available during the legislative session held in the calendar year before the tax expenditure is scheduled to repeal. The state auditor may revise the schedule so long as the state auditor continues to provide for a systematic evaluation of all tax expenditures, including any new tax expenditures enacted by the general assembly since the publication of a previous evaluation report, and so long as each tax expenditure is reviewed at least once every five years.

(e) Notwithstanding section 2-3-103 (2), C.R.S., the state auditor shall present the results in the form of an evaluation report that the state auditor shall ensure is posted on the general assembly's website, and, notwithstanding section 24-1-136 (9), C.R.S., the state auditor shall deliver a copy of the report to the joint budget committee and the finance committees of the senate and the house of representatives. The state auditor shall ensure the first evaluation report is delivered and posted no later than September 14, 2018, and shall ensure subsequent evaluation reports are delivered and posted no later than September 15 of each year thereafter.

(2) (a) Any records, information, or documentation generated pursuant to this section are work papers of the state auditor and shall be open to public inspection only upon approval of a majority of members of the legislative audit committee created in section 2-3-101, C.R.S. Only the specific work papers that the legislative audit committee votes to approve for disclosure shall be open to public inspection. Work papers that have not been specifically approved for disclosure by a majority vote of the legislative audit committee shall remain confidential. Under no circumstances shall the work papers be open to public inspection prior to a completed report being posted as specified in paragraph (e) of subsection (1) of this section.

(b) The department of revenue must provide any requested information, analysis, or data, if available and under the control of the department, as requested by the state auditor; except that, if the request includes confidential information, such information must remain confidential in the hands of the state auditor, and the state auditor is subject to the same limitations specified in section 39-21-113.

(c) The state auditor's authority set forth in section 2-3-107, C.R.S., applies to the state auditor's evaluation set forth in this section.

APPENDIX B: Example of how tax expenditure evaluations would change if expedited evaluations are allowed

LONG-TERM LODGING EXEMPTION

EVALUATION RESULTS

WHAT IS THE TAX EXPENDITURE?

In 1959, the General Assembly established a sales tax on temporary lodgings and created the Long-Term Lodging Exemption at the same time. The exemption has remained substantially unchanged since that time. According to Section 39-26-104(1)(f), C.R.S., sales of lodgings that are typically used for short-term stays, such as hotels, home shares, guesthouses, and trailer parks, are generally subject to state sales tax. However, under the Long-Term Lodging Exemption [Section 39-26-704(3), C.R.S.], sales of lodgings for stays of 30 consecutive days or more are tax exempt. In addition, eligible lodging purchases are exempt from local sales taxes, including lodging taxes, in cities and counties that have their local sales taxes collected by the State on their behalf. This is because statute [Section 29-2-105(1)(d)(I), C.R.S.] mandates that these local governments apply most of the State's sales tax exemptions, including the Long-Term Lodging Exemption. Home-rule cities established under Article XX, Section 6 of the Colorado Constitution that collect their own sales taxes have the authority to set their own tax policies independent from the State and are not required to exempt long-term lodging from their local sales tax, although many choose to do so.

For a sale to be eligible for the exemption, there must be a written agreement for occupancy between the purchaser and lodging provider, which can include a receipt or a hotel registration, and the same payee must pay for the duration of the stay, which must be at least 30 consecutive days. If the price of the stay is not paid in full up-front, or is paid up-front but is refundable, Department of Revenue guidance indicates that lodging providers can either not collect the

sales tax, in which case they would be liable for the sales tax if the customer does not complete at least a 30-day stay, or collect the tax and then refund it after the customer has stayed at least 30 days. In some cases, the customer may have to apply to the Department of Revenue for a refund if they stay for at least 30 days, but the lodging provider collects the sales tax and does not refund it. Lodging providers must have a sales tax license and report the value of the Long-Term Lodging Exemption on the Department of Revenue's Retail Sales Tax Return (Form DR 0100) using the "other exemptions" line of the form's exemptions schedule. This line aggregates several exemptions that do not have a separate reporting line on the form.

For expedited reviews we would conduct less background research, so some details, like this information from a US Census Bureau report would be cut.

WHO ARE THE INTENDED BENEFICIARIES OF THE TAX EXPENDITURE?

Statute does not explicitly identify the intended beneficiaries of this exemption. Based on the statutory language of the exemption, we inferred that the intended beneficiaries of this exemption are individuals and businesses who purchase long-term stays in lodgings, such as hotels, corporate housing, home shares (including online platforms such as Airbnb, Vacation Rentals by Owners (VRBO), and HomeAway), recreational vehicle parks, and campgrounds, which are typically subject to state sales tax. ~~According to a 2006 study conducted by the U.S. Census Bureau, individuals who occupy hotels on a long-term basis do so for a variety of reasons, including, financial hardship that results in the loss of permanent housing, relocation by an employer on a temporary or permanent basis, loss of a home to fire or natural disaster, or a decision to live in high-end hotels to have access to luxury services. Some of these individuals choose hotels specifically designed and marketed for extended stays, but others stay in traditional hotels, some of which may offer low rates and flexible payment terms (e.g., discounted weekly rates, day-to-day payments) targeted to individuals experiencing financial hardship.~~

WHAT IS THE PURPOSE OF THE TAX EXPENDITURE?

Statute does not explicitly state the purpose of this exemption. Because it was enacted in 1959, concurrently with the state sales tax on lodging, we inferred that the purpose was to limit the state sales tax on lodging to individuals making

short-term stays (less than 30 days) and provide parity in tax treatment between people who enter into residential leases for 30 days or more (which are not subject to sales tax) and people making long-term stays at lodging establishments which are more typically used for short-term stays by travelers.

IS THE TAX EXPENDITURE MEETING ITS PURPOSE AND WHAT PERFORMANCE MEASURES WERE USED TO MAKE THIS DETERMINATION?

Because the Department of Revenue does not store information from taxpayers specific to the Long-term Lodging Exemption in GenTax, its tax reporting and information system, we did not assess whether this exemption is accomplishing its purpose or the extent to which it is applied by lodging providers. However, the Department of Revenue has issued guidance for lodging providers on how to apply the exemption, which may increase the likelihood that they are applying it to long-term stays.

For expedited reviews, we would not do additional research and analysis to conclude on whether the expenditure is meeting its purpose, unless such information was readily available.

~~We determined that this exemption is accomplishing its purpose for many long-term occupants of lodgings, but some lodging providers may not consistently apply it. Statute does not provide quantifiable performance measures for this tax expenditure. Therefore, we created and applied the following performance measure to determine the extent to which the exemption is meeting its inferred purpose.~~

~~**PERFORMANCE MEASURE:** *To what extent are the amounts paid for long-term lodgings being exempted from sales tax?*~~

~~**RESULT:** Although we lacked adequate data to quantify the extent to which customers who make stays of 30 days or more in otherwise taxable lodgings are properly exempted from state and local sales tax, we determined that the exemption is likely applied to a substantial portion of lodging sales. Specifically, based on our analysis of Department of Revenue data and information from lodging providers, we estimate that the exemption was applied to $423 million (10 percent) of about $4.3 billion in total retail lodging sales in the state (see discussion below on how we arrived at our revenue estimates), which indicates that the exemption is frequently used. However, we did not have information~~

~~on what percentage of stays were for 30 consecutive days or more, and therefore eligible for the exemption.~~

~~Despite evidence that the exemption is frequently used, we also found that lodging providers may not consistently apply the Long-Term Lodging Exemption, which could reduce the extent to which long-term stays are exempted from sales tax. Specifically, we found the following based on our review of several types of lodging providers:~~

- ~~**TRADITIONAL HOTELS.** We called a non-statistical sample of 20 Colorado hotels, including several large hotel chains, and customer service representatives at eight of the hotels indicated that they would not charge sales tax for a planned stay of 30 or more days (40 percent). Of the remaining 12 hotels that indicated that they would charge the sales tax, two stated that they would only apply the exemption for stays of 31 days or more and the other 10 did not seem to be aware of the exemption.~~

- ~~**EXTENDED STAY HOTELS.** We reviewed the online booking systems of five extended stay hotels and found that three did not include sales taxes in their quoted price for a planned stay of 30 or more days, the other two included the sales tax in the quoted price. We contacted each hotel and staff at all five indicated that the tax would be refunded or credited to a guest's account after 30 days.~~

- ~~**CORPORATE HOUSING.** We interviewed representatives from two corporate housing providers that specialize in providing accommodations, such as furnished apartments, for long-term business travelers, and both indicated that they apply the exemption to stays of 30 or more days.~~

- ~~**HOME SHARES.** We reviewed the websites of Airbnb, VRBO, and HomeAway, the three largest home share platforms. We found that as of March 2018, Airbnb's website applies the exemption correctly to the quoted price of most long-term stays, although it appears to require a stay of 31 or more days before removing sales taxes. VRBO and HomeAway typically place the responsibility of sales tax collection and remittance on the lodging owners and there was no data available to determine the extent to which~~

~~they apply the exemption.~~

~~Though our assessment of the practices of lodging providers suggests that some may improperly collect sales tax from customers making long-term stays, we did not inform the providers that we contacted that we would expect them to exempt long-term stays from sales tax. Thus, it is possible that if a customer knew that the exemption should apply and asked the lodging providers' customer service representatives to remove or refund the sales tax, the providers would do so. However, based on our limited survey of hotels in the state, it appears that lodging customers who are unaware of the exemption may be charged sales tax by some lodging providers.~~

Expedited reviews would have limited analysis of the economic costs and benefits, unless such information is readily available.

WHAT ARE THE ECONOMIC COSTS AND BENEFITS OF THE TAX EXPENDITURE?

~~We estimate that about $12.3 million in state revenue was forgone in Calendar Year 2017 as a result of the Long-Term Lodging Exemption. As shown in EXHIBIT 1.1, we calculated the revenue impact estimate separately for the hotel and corporate housing industry sectors due to different data sources for each sector.~~

~~EXHIBIT 1.1.~~
~~ESTIMATED REVENUE IMPACT OF THE LONG-TERM LODGING EXEMPTION~~
~~BY LODGING INDUSTRY SECTOR~~
~~CALENDAR YEAR 2017~~

	~~SALES ATTRIBUTABLE TO LONG-TERM STAYS (30 DAYS OR MORE)~~	~~STATE REVENUE IMPACT~~	~~LOCAL GOVERNMENT REVENUE IMPACT~~	~~TOTAL REVENUE IMPACT~~
~~Hotels and Home Shares[1]~~	~~$356 million~~	~~$10.3 million~~	~~$6.6 million~~	~~$16.9 million~~
~~Corporate Housing[2]~~	~~$67.3 million~~	~~$2 million~~	~~$1.3 million~~	~~$3.3 million~~
~~TOTAL~~	~~$423.3 million~~	~~$12.3 million~~	~~$7.9 million~~	~~$20.2 million~~

~~SOURCE: Office of the State Auditor analysis of data from the 2015 Department of Revenue reports, State Demographer data, Bureau of Economic Analysis data, and information published by industry associations.~~

~~[1] Data provided in the Department of Revenue 2015 Retail Sales Tax Reports.~~

~~[2] Data provided by Corporate Housing Providers Association. Assumes that all corporate housing stays are 30 days or longer.~~

~~To arrive at the revenue impacts, we first estimated the total taxable revenue associated with long-term lodging stays of 30 days or more. We used data from the Department of Revenue's 2015 Retail Sales Tax Reports to determine that hotels and other types of accommodations, such as home shares, reported $450.6 million in tax exempt sales (the difference between net sales and taxable sales on their Retail Sales Tax Returns) in Calendar Year 2015 (the most recent year available), which includes exempt sales for lodging and other items, such as food. Although the Department of Revenue does not collect data specifically for the Long-Term Lodging Exemption on its Retail Sales Tax Return (Form DR 0100), our review of the State's sales tax exemptions indicates that this exemption is likely the most common exemption that would apply to sales of lodging. There are no other sales tax exemptions specifically targeted to the lodging industry and only a few other exemptions appear to potentially apply to the lodging providers, such as exemptions on food sold through vending machines (Section 39-26-714(2), C.R.S.), and food provided to restaurant staff (Section 39-26-707(2)(a), C.R.S). We attributed a factor of 25 percent to these nominal other exemptions. Therefore, we assumed that 75 percent of the tax exempt sales reported by lodging providers were due to the Long-Term Lodging Exemption. We multiplied this figure by the $450.6 million in reported exempt sales, to estimate $337.9 million in Long-Term Lodging Exemptions for Calendar Year 2015. We then increased this amount by 5.3 percent to account for growth in the hotel industry from Calendar Year 2015 to 2017, as reported by the U.S. Bureau of Economic Analysis, to arrive at our estimate of $356 million in exempted sales for the hotel and home share sector.~~

~~Because corporate housing providers may not be included with hotels and other types of accommodations in the Department of Revenue's retail sales tax reports, we obtained sales revenue data from the Corporate Housing Providers Association, which showed total U.S. corporate housing revenues of $3.2 billion in Calendar Year 2016. We multiplied this figure by 2.1 percent, which is the share of U.S. hotel sales that occurred in Colorado in 2012, which is the most recent year available, to estimate $65.9 million in Colorado corporate housing sales. We then increased this amount by 2 percent to account for industry growth and inflation from Calendar Year 2016 to 2017, as reported by the U.S. Bureau of Economic Analysis, to arrive at our estimate of $67.3 million in Colorado corporate housing sales for Calendar Year 2017. We~~

~~assumed that all of these sales were exempt under the Long-Term Lodging Exemption because according to the stakeholders we contacted, it is uncommon for corporate housing units to be used for shorter-term stays, though a few shorter-term stays could be included in our estimate and cause a slight overestimate.~~

~~To estimate revenue impacts, we then applied the State's 2.9 percent sales tax rate and the Colorado population-weighted average local tax rate (including lodging taxes, if applicable) of 1.95 percent, which excludes self-collected home-rule cities, to our revenue estimates discussed above.~~

~~It is important to note that our estimated revenue impacts could double count the impact associated with corporate housing providers to some degree because we could not determine how corporate housing providers are typically categorized in the Department of Revenue's Retail Sales Tax Reports. Specifically, these reports rely on self-reported information from taxpayers based on the North American Industry Classification system. It is possible that some corporate housing providers could have selected industry categories that would have included them within the "Hotels and Other Accommodation Services" category in the Department of Revenue reports, the category we used to estimate the revenue impact from hotels and home shares, as opposed to other categories, such as the "Real Estate, Rental and Leasing." In this case, our estimate would likely double count the revenue impact.~~

~~The savings provided by the exemption may provide a significant benefit to some individuals, but likely has only a small impact on the lodging industry in general.~~ *We lacked readily available information to estimate the overall revenue impact of the exemption to the State and to local governments, though the savings provided by the exemption may provide a significant benefit to some individuals.* Specifically, for some individuals, the combined state and local tax savings, which averages 4.85 percent ~~and $20.2 million in total~~, or about $146 on a 30-day $100 per night hotel stay, may be significant enough to drive choices about where they make overnight stays. In particular, individuals who are staying in hotels due to economic hardship may choose or only be able to afford to stay in a hotel because of the cost savings provided by the exemption. Further, in some local jurisdictions with higher tax rates on lodging, which can range up to 9.5 percent,

the exemption may be more important to price-sensitive customers. In addition, for many individuals who choose to make long-term stays in hotels and other lodging establishments, other forms of housing, such as apartment or home leases, which are typically less expensive on a monthly basis, are impractical. This can be the case when individuals do not wish to enter into typical 6-month or 1-year lease terms, require hotel services and amenities, cannot pay the required up-front deposits that are often required for leases, or have poor credit.

~~For the lodging industry, the $20.2 million in estimated total cost savings to consumers represents about 0.5 percent of the $4.3 billion in total lodging sales in Calendar Year 2017. Therefore, the exemption likely has a relatively small impact on the lodging industry as a whole, since even if consumers used all of their cost savings on longer or more expensive hotel stays, it would represent a small increase in industry sales. However,~~ In addition, the exemption may ~~be more~~ *provide a* significant incentive for businesses that specialize in long-term lodging, such as corporate housing providers, or extended stay hotels. In particular, because most states have a similar exemption, the Long-Term Lodging Exemption could also help keep long-term lodging providers in Colorado competitive for individuals who have the flexibility to choose which state to stay in.

WHAT IMPACT WOULD ELIMINATING THE TAX EXPENDITURE HAVE ON BENEFICIARIES?

Eliminating the exemption could increase the cost of long-term lodging, result in unequal tax treatment of people depending on the type of long-term lodging they purchase, and negatively impact lodging providers who specialize in long-term accommodations. Specifically, without the exemption, the after-tax cost of long-term stays in non-home rule jurisdictions would increase, on average, by 4.85 percent due to state and local taxes. However, some lodging establishments could choose to offset part of this increase by reducing prices to remain competitive with establishments that are subject to lower taxes, since local tax rates for lodging vary considerably across the state. In addition, individuals who reside in lodgings, such as hotels, corporate housing, and home shares, on a long-term basis would pay sales taxes that do not apply to individuals who enter into traditional residential leases. This could create a hardship for some individuals who cannot enter into

traditional leases and could cause some businesses to choose alternative means of housing, such as renting apartments, for employees that need to make stays of over 30 days.

Several industry representatives we interviewed stated that the Long-Term Lodging Exemption is important to their businesses and to Colorado's lodging industry. Corporate housing providers reported that they are able to remain competitive with similar businesses and the hotel industry as a result of the exemption, and the same may be true for other lodging providers that rely on long-term occupants. Members of a lodging providers association predicted that eliminating the exemption would be damaging to their businesses and may have other adverse effects, such as driving up housing costs or causing some low-income residents to move to states where their dollar would stretch further.

ARE THERE SIMILAR TAX EXPENDITURES IN OTHER STATES?

At least 46 states assess a sales or lodging tax on the price of temporary lodgings and at least 41 of these states provide an exemption for long-term lodgings. However, the minimum length of occupancy required to qualify for a "long-term" lodging exemption varies by state, and can be anywhere from 28 days to 185 days. The most common time period was 30 days, which is the requirement in Colorado.

ARE THERE OTHER TAX EXPENDITURES OR PROGRAMS WITH A SIMILAR PURPOSE AVAILABLE IN THE STATE?

We did not identify any similar tax expenditures or programs in Colorado.

WHAT DATA CONSTRAINTS IMPACTED OUR ABILITY TO EVALUATE THE TAX EXPENDITURE?

The Department of Revenue does not track the amount of Long-Term Lodging Exemptions claimed by lodging providers. Specifically, the Department of Revenue's Retail Sales Tax Return (Form DR 0100), does not contain a specific line for long-term lodging sales, and lodging providers report the sales that qualify for this exemption as part of the "other exemptions" line on the form, which combines any exemption not specifically addressed

elsewhere on the form. Since this line can encompass several different exemptions, the Department of Revenue does not capture this data point in GenTax, its tax reporting system. If the General Assembly wants to know the amount of the exemption claimed with a higher degree of reliability than the estimates provided in this evaluation, it could require the Department of Revenue to add a specific line to the DR 0100 where lodging providers are required to report this information and direct the Department of Revenue to capture these data in GenTax. However, this change could increase the administrative burden on lodging providers who would be required to separately track long-term lodging sales and the amount exempted. It would also require resources for the Department of Revenue to update the form, provide new instructions, and make programming changes in GenTax to capture the information (see the Tax Expenditures Overview section of this Compilation Report for details on limitations of Department of Revenue data and potential costs for addressing them).

WHAT POLICY CONSIDERATIONS DID THE EVALUATION IDENTIFY?

THE GENERAL ASSEMBLY COULD CONSIDER CLARIFYING WHETHER THE EXEMPTION SHOULD BE AVAILABLE TO THIRD-PARTY PAYERS. Statute specifies that the Long-Term Lodging Exemption is for sales that are made "to any occupant who is a permanent resident" of the lodgings [Section 39-26-704(3), C.R.S.]. Statute does not indicate whether this should apply to third-party payer situations, such as when a business pays for a room that is occupied by multiple employees over the length of stay. However, the current Department of Revenue policy is to allow the exemption under such circumstances so long as the lodgings are paid for by the same payer for at least 30 consecutive days, regardless of whether the lodgings are actually occupied by the same person for that length of time. The Department of Revenue's policy likely decreases the administrative burden on lodging providers and taxpayers, but also allows for a broader application of the exemption than may have been intended and likely increases its revenue impact.

THE GENERAL ASSEMBLY COULD CONSIDER CLARIFYING WHETHER HOME-SHARES AND SIMILAR FORMS OF LODGING SHOULD QUALIFY FOR THE

EXEMPTION. With the expansion of the home sharing industry, non-traditional temporary lodging options are growing. ~~Although we found that, in practice, some home-share sales are being exempted from sales tax under the Long-Term Lodging Exemption~~ However, statute [Section 39-26-704(3), C.R.S.] does not specifically list "home-shares" or "private homes" as an exempted category of lodgings. Such sales could be interpreted as falling under categories that are listed, such as "guesthouse" or "lodging house," though it may not be clear to some taxpayers how to interpret these terms.

~~More broadly, while Airbnb collects Colorado sales tax on behalf of home-share hosts, hosts operating through other platforms may not be clear about whether or not they are liable for sales tax for any sales, even those under 30 days. Specifically~~ Similarly, statute [Section 39-26-102(11), C.R.S.] does not include accommodation sales of "home-shares" or "private homes" in the list of lodging types which are subject to sales tax. Similar to the language in the Long-Term Lodging Exemption, "guesthouse" and "lodging house" are included as applicable lodging types and could be interpreted as including such sales; however, the General Assembly could consider clarifying the types of lodging sales that are subject to sales tax.

2018 Tax Expenditure Compilation Report

Joint Budget Committee

November 15, 2018

Colorado Office of the State Auditor

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SB 16-203: Our Mandate

"Provide the State with factual evidence of whether the State's tax expenditures achieve the objectives they are intended to achieve."

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First Step:
Identify Tax Expenditure Provisions

- 216 total
- 40 are 50+ years old
- 22 will eventually expire with no legislative action.
- 194 are permanent
- $5.4 billion revenue impact annually (2013 DOR estimate)

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How did the OSA Evaluate Tax Expenditures?

- 15 reviewed in 2018
- Key statutory requirements
  - Assess whether each is meeting its purpose
  - Analyze the economic costs and benefits (revenue impact)
  - Evaluate the impact on intended beneficiaries
  - Report data constraints
  - Identify policy considerations to improve effectiveness and administration

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What is the purpose of the tax expenditure?

- Only 1 of 15 had a direct statement of purpose in statute
- None had performance measures in statute
- For most, we inferred a purpose and created performance measures

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Economic Costs and Benefits

- $0 to $4.2 billion
- Some “not reportable” or “could not determine”

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Policy Considerations

- 12 of 15 had policy considerations
  - Consider repeal because they are no longer used (3)
  - Clarify statute (6)
  - Review to improve administration or effectiveness (3)

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Data Constraints

- 11 of 15 evaluations impacted by data constraints
- Common DOR data issues:
  - Not captured on a DOR form
  - Multiple expenditures aggregated on reporting lines
  - Information on forms is not easily extracted from GenTax
  - Tax Information is self-reported by taxpayers
  - Tax information changes over time
- Use of third-party data

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What's coming for 2019?

- Quarterly reporting format
- Evaluations scheduled for release in January 2019:
  - Aircraft used outside the state by on-demand air carriers exemption
  - Credit for health preceptors working in shortage areas
  - Childcare expense tax credits
  - Historic property preservation credit
  - Two insurance tax expenditures—the Fraternal Benefits Exemption, and Gross Premiums Deduction

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Hunger Relief Income Tax Credit & Crop and Livestock Income Tax Credit

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Hunger Relief Income Tax Credit & Crop and Livestock Income Tax Credit

HOW TO CLAIM THE CREDITS:

FARMER HAS EXTRA FOOD TO DONATE

FARMER CALLS FOODBANK AND THEY ARRIVE WITH A TRUCK

THE FOODBANK ISSUES THE FARMER A DONATION CERTIFICATE

THE FARMER SUBMITS THE CERTIFICATE TO THE DEPARTMENT OF REVENUE TO CLAIM THE CREDIT

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Hunger Relief Income Tax Credit & Crop and Livestock Income Tax Credit

	Hunger Relief Credit, CY 2016	Crop and Livestock Credit, CY 2012-2016
Year Enacted	2014	1982
Repeal/Expiration Date	January 1, 2020	None
Revenue Impact	$71,000	Minimal
Number of Taxpayers Claiming	353	Too few to report
Average Taxpayer Benefit	$201	Too few taxpayers to report
Is it Meeting its Purpose?	Yes, but the impact is relatively small	No, because it has been used infrequently

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Hunger Relief Income Tax Credit & Crop and Livestock Income Tax Credit

AG DONATIONS TO COLORADO FOOD BANKS VS. PRODUCE SOURCED AND DISTRIBUTED TO FOOD BANKS ACROSS COUNTRY			
FOOD BANK	2014	2016	PERCENT CHANGE
Feeding America Network of Food Banks	970 million	1.25 billion	**29%**
5 Colorado Food Banks	24 million	35 million	**47%**
Max Amount of 2014-2016 Increase Due to Hunger Relief Credit	1.5 million pounds		

SOURCE: Office of the State Auditor analysis of data provided by Feeding Colorado and Feeding America.

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Hunger Relief Income Tax Credit & Crop and Livestock Income Tax Credit

HUNGER RELIEF CREDIT SCENARIOS BY ADDITIONAL POUNDS DONATED IN CALENDAR YEARS 2015 AND 2016 AND DOLLARS-PER-POUND STATE IS "PAYING"		
Percent of Donations Incentivized by Credit	Pounds Donated Attributable to Credit	Cost per pound to the State
5 Percent	146,000	$1.44
10 Percent	293,000	$0.72
20 Percent	585,000	$0.36
21 Percent	**614,000**	**$0.34 (Break Even)**
30 Percent	878,000	$0.24

SOURCE: Office of the State Auditor analysis of Department of Revenue data for Tax Years 2015 and 2016 and food bank receipts for Calendar Year 2015-2017.

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Hunger Relief Income Tax Credit & Crop and Livestock Income Tax Credit

- Lack of awareness of the credits across agricultural community
- Many agricultural producers' tax liabilities are too low to benefit from the Hunger Relief Credit
- Requirement for agricultural producers to file a Schedule F to claim Hunger Relief credit may be reducing number claiming credit
- Crop and Livestock Credit's $1,000 cap may be too low to incentivize C corporations to claim credit

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Long-Term Lodging Sales Tax Exemption

VRBO®

airbnb

HomeAway®

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Long-Term Lodging Sales Tax Exemption

ESTIMATED REVENUE IMPACT OF THE LONG-TERM LODGING EXEMPTION BY LODGING INDUSTRY SECTOR CALENDAR YEAR 2017				
	Sales Attributable to Long-Term Stays (30 days or more)	State Revenue Impact	Local Government Revenue Impact	Total Revenue Impact
Hotels and Home Shares[1]	$356 million	$10.3 million	$6.6 million	$16.9 million
Corporate Housing[2]	$67.3 million	$2 million	$1.3 million	$3.3 million
TOTAL	$423.3 million	**$12.3 million**	$7.9 million	$20.2 million

SOURCE: Office of the State Auditor analysis of data from the 2015 Department of Revenue reports, State Demographer data, Bureau of Economic Analysis data, and information published by industry associations.

[1] Data provided in the Department of Revenue 2015 Retail Sales Tax Reports.

[2] Data provided by Corporate Housing Providers Association. Assumes that all corporate housing stays are 30 days or longer.

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Long-Term Lodging Sales Tax Exemption

Exemptions Schedule- Part B (Exemptions vary, refer to Colorado Sales

This schedule is required for exemptions claimed on line 3b, page 1.

	State	RTD/CD	Special District
	(B1-1)	(B1-2)	(B1-3)
1. Food, including food sold through vending machines	.	.	.
	(B2-1)	(B2-2)	(B2-3)
2. Machinery	.	.	.

⋮

	(B0-1)	(B0-2)	(B0-3)
10. Other Exemptions, explanation required	.	.	.
Explain			

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Long-Term Lodging Sales Tax Exemption

- *"There shall be exempt from taxation under the provisions of part 1 of this article all sales and purchases of commodities and services under the provisions of section 39-26-102(11) to any occupant who is a permanent resident of any hotel, apartment hotel, lodging house, motor hotel, guesthouse, guest ranch, trailer coach, mobile home, auto camp, or trailer court or park and who enters into or has entered into a written agreement for occupancy of a room or accommodations for a period of at least thirty consecutive days during the calendar year or preceding year."*

[Section 39-26-704(3), C.R.S.]

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Biogas Production Components Sales Tax Exemption

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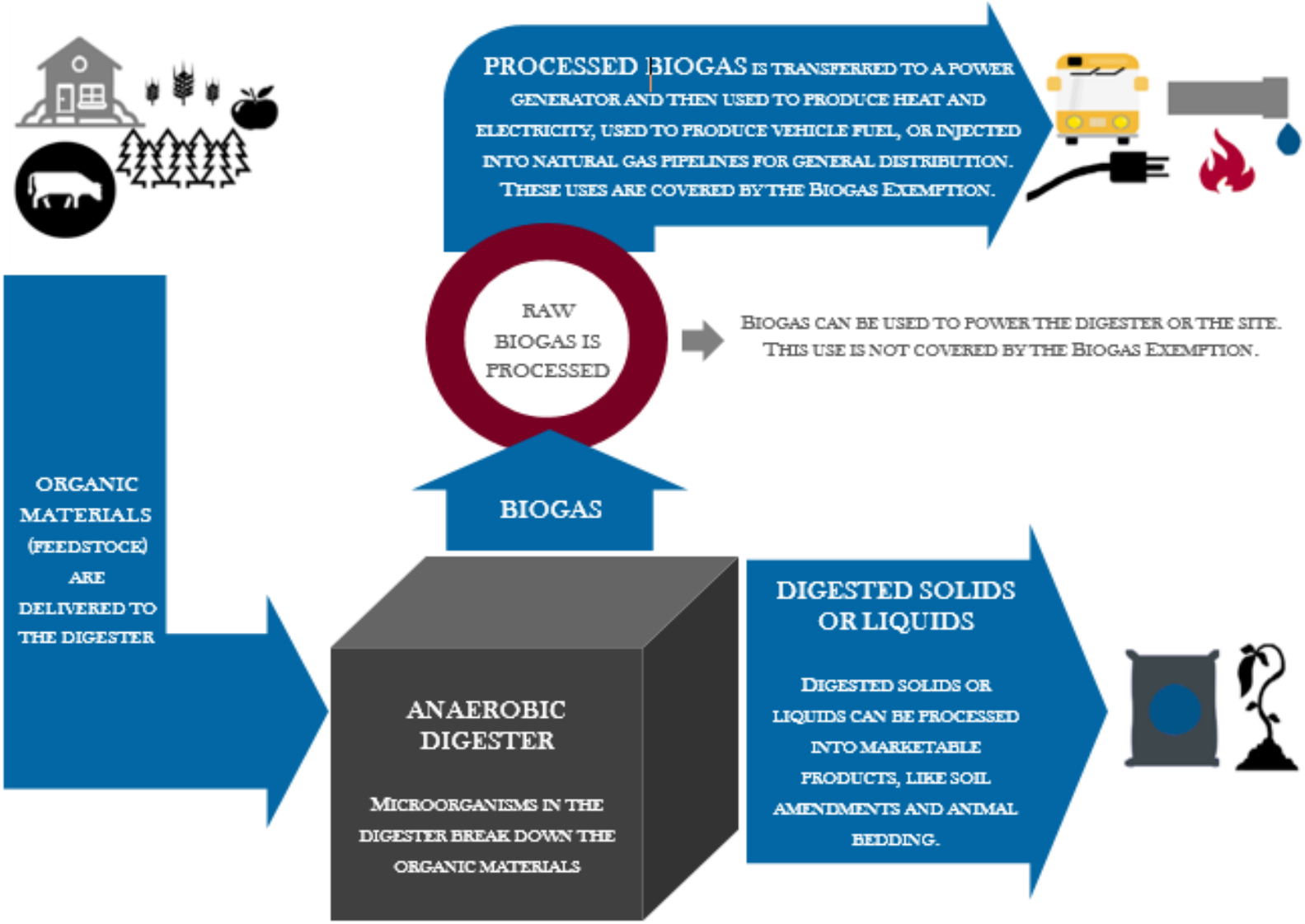
Biogas Production Components Sales Tax Exemption



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Biogas Production Components Sales Tax Exemption

EXHIBIT 1.3. ESTIMATED TAXPAYER SAVINGS FOR PROJECT SCENARIOS				
PROJECT COST RANGE	TOTAL INCURRED CAPITAL EXPENSES	PERCENTAGE OF CAPITAL EXPENSES ELIGIBLE FOR EXEMPTION	EXPENSES ELIGIBLE FOR EXEMPTION	TAXPAYER SAVINGS
SCENARIO 1: Small, Onsite System	$1,000,000	40%	$400,000	$11,600
SCENARIO 2: Small, Onsite System	$1,000,000	75%	$750,000	$21,750
SCENARIO 3: Large, Stand-alone System	$30 million	40%	$12 million	$348,000
SCENARIO 4: Large, Stand-alone System	$30 million	75%	$22.5 million	$652,500
SOURCE: Office of the State Auditor analysis of industry reports and stakeholder feedback.				

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Biogas Production Components Sales Tax Exemption

EXHIBIT 1.4. ESTIMATED IMPACT TO STATE REVENUE, THROUGH JULY 2018	
TOTAL PROJECT COST	$102 MILLION
Minimum estimated amount spent on biogas production components (40 percent of total project cost)	$40.8 million
Maximum estimated amount spent on biogas production components (75 percent of total project cost)	$76.5 million
Colorado retail sales tax rate	2.9%
Minimum revenue impact resulting from exemption	$1.2 million
Maximum revenue impact resulting from exemption	$2.2 million
SOURCE: Office of the State Auditor analysis of estimated project costs reported in news articles and legal filings.	

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