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Fiscal Note

Drafting Number: LLS 21-0171 Date: April 01, 2021
Prime Sponsors: Rep. Larson Bill Status: House Education
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Bill Topic: MODIFICATIONS TO QUALIFIED STATE TUITION PROGRAMS

- Summary of Fiscal Impact:
[X] State Revenue [] TABOR Refund
[X] State Expenditure [] Local Government
[] State Transfer [] Statutory Public Entity

The bill creates the foundational learning experience savings program, which allows individuals to create a tax-preferred savings account for elementary and secondary education expenses. It decreases state revenue on an ongoing basis, and increases state expenditures in FY2021-22.

Appropriation Summary: No appropriation is required.

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

Table 1
State Fiscal Impacts Under HB 21-1210

Table with 4 columns: Category, Budget Year FY 2021-22, Out Year FY 2022-23, Out Year FY 2023-24. Rows include Revenue (General Fund), Expenditures (CollegInvest Administration), Transfers, and TABOR Refund.

Summary of Legislation

The bill creates the foundational learning experience (FLEX) savings program within the Department of Higher Education. Under the FLEX program, individuals can create a tax-preferred savings account with CollegeInvest. Funds from the account can be used to pay for qualified elementary and secondary tuition expenses. Distributions from a FLEX savings account are exempt from state taxable income.

Owners of both a college savings account (“529 account”) and a FLEX account may move money between the two accounts. The total amount transferred from a college savings account to a FLEX account may not exceed \$10,000, and individual transfers may not exceed the college savings account’s lowest balance during the last two years. Transfers from a FLEX account to a college savings account are not limited.

The bill also changes the definition of qualified higher education expenses under a section 529 account to include expenses related to apprenticeship programs. Further, the bill clarifies that qualified higher education expenses do not include student loan repayments.

Background

Under current state law, a taxpayer may deduct contributions to a 529 account for qualified higher education expenses when computing their Colorado taxable income. Effective in 2018, federal law was amended to allow 529 accounts to be used to pay up to \$10,000 annually for K-12 education at public, private, or religious schools. However, under Colorado law, expenditures for K-12 education from 529 accounts are considered non-qualified withdrawals and therefore subject to recapture of tax, penalty, and interest. Investment income earned in a 529 account is not taxed at either the federal or state level.

Unlike 529 account contributions, under this bill contributions to a FLEX account are not eligible for a state or federal deduction. However, funds may be transferred from 529 accounts to FLEX accounts, thereby allowing contribution deductions if funds are first contributed to 529 accounts.

Assumptions

Because contributors may transfer funds from a 529 account to a FLEX account, the fiscal note assumes that some portion of taxpayers will route their contributions to a FLEX account through a 529 account, allowing them to deduct their contributions from their state taxable income. Further, while contributions directly to a FLEX account are not deductible from state taxable income, any investment income generated from these accounts would be exempt from state taxable income. Assuming that without this bill, families would save the same amount annually in a non-tax-preferred account and earn a similar return, the bill results in decreased tax revenue due to the new exemption for investment income from a FLEX account.

Based on data from the Colorado Department of Education, there were approximately 51,270 children enrolled in private school for the 2019-2020 school year. Assuming on average there are 1.85 children per family in Colorado, there are approximately 27,710 families with children enrolled in private

school. The fiscal note assumes that approximately 15 percent of these families, or about 4,160 families, will participate in the FLEX program in the first year, with participation growing by 10 percent in subsequent years. Furthermore, the fiscal note assumes an average annual contribution to FLEX savings accounts of \$4,380 per family, which is approximately half of the average annual contribution to a 529 account as private school tuition is roughly half the cost of college tuition. Contributions within a FLEX savings account are assumed to grow six percent annually, and individuals withdraw a quarter of their account balance each year for tuition expenses.

State Revenue

The bill is expected to decrease General Fund revenue by up to \$414,460 in FY 2021-22 (half-year impact), by up to \$911,810 in FY 2022-23, and by up to \$407,715 in FY 2023-24. These amounts represent an upper bound and assume that taxpayers' contributions to their FLEX accounts are first deposited in a 529 account and then up to the maximum \$10,000 per recipient is transferred to a FLEX account in order to maximize tax savings. Revenue impact amounts reflect an upper bound based on the Assumptions section of this fiscal note and the \$10,000 limitation on transfers between accounts begins to limit the upper bound beginning in FY 2023-24. The timing of contributions and extent to which taxpayers make transfers from 529 accounts to FLEX accounts will influence the timing and amount of revenue impacts.

If taxpayers do not route FLEX contributions through a 529 account, state revenue will decrease by up to \$24,870 in FY 2021-22 and \$92,010 in FY 2022-23 as a result of tax savings on investment income only. The bill is expected to decrease income tax revenue, which is subject to TABOR.

State Expenditures

The bill is expected to increase workload for the Department of Higher Education and increase expenditures for CollegeInvest in FY 2021-22.

Department of Higher Education. In FY 2021-22, the bill increases workload for the Department of Higher Education to update their website to include the new FLEX program and potentially answer inquiries from the public. This increase in workload can be accomplished within existing appropriations.

CollegeInvest. In FY 2021-22, the bill increases expenditures for CollegeInvest by \$650,000 to implement the new FLEX savings accounts. No appropriation is necessary as CollegeInvest will use their own administrative funds for any costs associated with the bill.

TABOR refunds. The bill decreases state revenue subject to TABOR. For FY 2022-23, the March 2021 LCS forecast projects revenue to fall short of the TABOR limit by \$28.6 million, or 0.2 percent of the limit. If actual revenue exceeds the limit, the bill will decrease the amount required to be refunded to taxpayers from the General Fund in FY 2023-24. If the bill causes revenue to fall below the limit by \$30 million, it will trigger a transfer of up to \$30 million from the Unclaimed Property Trust Fund to the Housing Development Grant Fund under current law enacted in House Bill 19-1322.

Effective Date

The bill takes effect January 1, 2022, assuming no referendum petition is filed.

State and Local Government Contacts

Higher Education
Information Technology

Revenue
Regulatory Agencies

Personnel