



Legislative Council Staff
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Fiscal Note

Drafting Number:	LLS 23-0727	Date:	January 30, 2023
Prime Sponsors:	Rep. Bradfield; Ortiz	Bill Status:	House Finance
		Fiscal Analyst:	Elizabeth Ramey 303-866-3522 elizabeth.ramey@coleg.gov

Bill Topic: CONTINUATION OF MILITARY RETIREMENT BENEFIT DEDUCTION

Summary of Fiscal Impact:	<input checked="" type="checkbox"/> State Revenue	<input checked="" type="checkbox"/> TABOR Refund
	<input checked="" type="checkbox"/> State Expenditure	<input type="checkbox"/> Local Government
	<input type="checkbox"/> State Transfer	<input type="checkbox"/> Statutory Public Entity

The bill extends the military retirement benefits deduction for taxpayers under age 55, which is currently set to expire after 2023, through 2033. It decreases state revenue through FY 2033-34.

Appropriation Summary: No appropriation is required.

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

Table 1
State Fiscal Impacts Under HB 23-1084

		Budget Year FY 2023-24	Out Year FY 2024-25
Revenue	General Fund	(\$2.2 million)	(\$4.4 million)
Expenditures		-	-
Transfers		-	-
Other Budget Impacts	TABOR Refund	(\$2.2 million)	(\$4.4 million)

Summary of Legislation

The bill extends the state income tax deduction for military retirement benefits received by taxpayers under age 55 for tax years 2024 through 2033 at the current law maximum deduction amount of \$15,000.

Background

Pension and annuity deduction. Colorado allows taxpayers to deduct federally taxable pension and annuity income from their taxable income. The deduction is limited to \$24,000 annually for those age 65 and over, and to \$20,000 for taxpayers age 55 to 64.

Military retirement income deduction for taxpayers under 55. Military retirement income is taxable by default. Veterans who receive disability payments pay tax on their military retirement benefits, but not their disability payments. House Bill 18-1060 created a state income tax deduction for military retirement income for tax years 2019 through 2023. The state deduction is allowed for taxpayers under age 55, as taxpayers who are 55 and over are eligible to claim the preexisting pension and annuity deduction. Under current law enacted in HB 18-1060, the state deduction is limited to \$15,000 for tax years 2022 and 2023.

The actual tax benefit received by the taxpayer depends on their taxable income and the state income tax rate, which is 4.40 percent for 2022 and future years. For example, a taxpayer who takes the maximum \$15,000 deduction for tax year 2022 reduces their tax liability by \$660.

The Department of Revenue reports that about 7,000 taxpayers deducted a total of \$49.2 million from their 2020 tax returns under HB 18-1060, reducing their income tax due by \$2.2 million at a tax rate of 4.55 percent. The deduction in 2020 was limited to \$7,500 per taxpayer.

Assumptions

The fiscal note assumes that the distribution of retirees across ages and ranks in Colorado is stable and reflects historical distributions, with a population of military retirees receiving military retirement benefits in Colorado of about 50,000, of whom 20 percent are aged 19 to 54. Following this assumption and the benefits paid to veterans of each rank, it is estimated that the bill will make up to \$146 million in military retirement benefits tax deductible in tax years 2024 and 2025, with actual deductions limited by retirees' taxable incomes after the application of the federal standard deduction or itemized deductions taken on federal returns.

Further, the estimates are consistent with the December 2022 Legislative Council Staff economic forecast for inflation, which drives an increase in expenditures through tax year 2025, after which modest decreases in the population of eligible veterans are expected to offset the impact of inflation-drive cost of living adjustments. Finally, these estimates assume that not all eligible military retirees will claim the exemption, either because of lack of awareness or insufficient taxable income, with 70 percent of military retirees under age 55 claiming the exemption.

State Revenue

The bill is expected to reduce General Fund revenue by \$2.2 million in FY 2023-24, a half-year impact, by \$4.4 million in FY 2024-25, by \$4.5 million in FY 2025-26, and by similar amounts in future years. The bill will decrease state revenue through tax year 2033, resulting in a half-year revenue impact for FY 2033-34, after which the deduction expires. The bill reduces income tax revenue, which is subject to TABOR.

The estimate for FY 2024-25 and subsequent years reflects a full-year impact of extending the deduction at the \$15,000 cap, as well as a decrease in inflation consistent with historical rates. The bill's revenue impact may grow or decline in subsequent years depending on the number of veterans receiving military retirement income as well as the rate of inflation.

Other Budget Impacts

TABOR refunds. The bill is expected to decrease the amount of state revenue required to be refunded to taxpayers by the amounts shown in the State Revenue section above. This estimate assumes the December 2022 LCS revenue forecast. A forecast of state revenue subject to TABOR is not available beyond FY 2024-25. Because TABOR refunds are paid from the General Fund, decreased General Fund revenue will lower the TABOR refund obligation, but result in no net change to the amount of General Fund otherwise available to spend or save.

Effective Date

The bill takes effect 90 days following adjournment of the General Assembly sine die, assuming no referendum petition is filed.

State and Local Government Contacts

Information Technology
Revenue

Military Affairs

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