



# MILITARY FAMILY RELIEF FUND GRANTS DEDUCTION

EVALUATION SUMMARY | JULY 2022 | 2022-TE27

TAX TYPE	Income	REVENUE IMPACT (2021)	\$9,775
YEAR ENACTED	2013	NUMBER OF TAXPAYERS (2021)	61
REPEAL/EXPIRATION DATE	None		

**KEY CONCLUSION:** The deduction clarifies that grants from the Military Family Relief Fund are not subject to Colorado income tax. However, data constraints prevented us from determining the extent to which recipients are aware of the deduction and have deducted their grants in practice.

## WHAT DOES THE TAX EXPENDITURE DO?

The Military Family Relief Fund Grants Deduction [Section 39-22-104(4)(p), C.R.S.] allows recipients of grants from the Military Family Relief Fund to deduct the amount of the grants they receive from their Colorado income if the amounts are included in federal taxable income.

## WHAT IS THE PURPOSE OF THE TAX EXPENDITURE?

Statute does not establish a purpose for this deduction. Based on testimony from the bill sponsor for House Bill 13-1024 during committee hearings, we considered a potential purpose: to clarify that recipients of grants from the Fund are not required to pay Colorado income tax on their grants.

## WHAT POLICY CONSIDERATIONS DID THE EVALUATION IDENTIFY?

The General Assembly may want to consider establishing a statutory purpose and performance measures for the deduction.



# MILITARY FAMILY RELIEF FUND GRANTS DEDUCTION

## EVALUATION RESULTS

### WHAT IS THE TAX EXPENDITURE?

The Military Family Relief Fund Grants Deduction [Section 39-22-104(4)(p), C.R.S.] allows recipients of grants from the Military Family Relief Fund (Fund) to deduct the grant amounts they receive from their Colorado income if the amounts are included in their federal taxable income.

The Fund was established by the General Assembly in 2005, and is administered by the Colorado National Guard Foundation, a 501(c)(3) nonprofit organization. It is funded solely by voluntary contributions made by taxpayers on their Colorado income tax returns. According to statute [Section 28-3-1501, C.R.S.], “grants from the military family relief fund are intended to help families defray the costs of food, housing, utilities, medical services, and other expenses that may be difficult to afford when a family member leaves civilian employment for active military duty, is on active military duty in a hostile fire zone, or is called to state active duty by executive order of the governor.” Prior to February 2022, service members who had applied to the Fund were eligible to receive grants up to \$1,000 per month; in February 2022, administrators of the fund reduced the maximum award to \$200 per month.

In order to receive a grant from the Fund:

- A service member of the Colorado National Guard or reservist must currently be on active military duty for a minimum of 30 days on mobilization from federal authority, as enumerated in the Armed Forces Code (Title 10 U.S.C.), or be called to state active duty by the

order of the Governor; be a resident of Colorado; and complete an application as required by the Colorado National Guard Foundation.

- An active duty service member of the U.S. military must have been deployed overseas and be in receipt of hostile fire pay or the equivalent; be stationed in Colorado as verified by their commanding officer; be a resident of Colorado; and complete an application as required by the Colorado National Guard Foundation.

This deduction was established by the General Assembly in 2013, by House Bill 13-1024. The deduction has remained unchanged since that time; however, minor changes have been made to statute regarding the administration of the Fund.

There is no dedicated line for this deduction on Colorado tax returns. Instead, taxpayers use Line 18 “Other Subtractions, explain below” on Form DR 0104AD (Subtractions from Income Schedule) to claim this deduction.

#### WHO ARE THE INTENDED BENEFICIARIES OF THE TAX EXPENDITURE?

Recipients of grants from the Fund are the intended beneficiaries of this deduction. According to statute [Section 28-3-1503, C.R.S.], the Fund may award grants to members of the Colorado National Guard or Reservists, active duty military personnel stationed in Colorado, or the families of the Colorado National Guard or reservists or active duty military personnel stationed in Colorado. In 2021, the fund disbursed a total of \$217,222 in grants to 61 applicants.

#### WHAT IS THE PURPOSE OF THE TAX EXPENDITURE?

Statute and the enacting legislation for the deduction do not state its purpose. Based on testimony from the bill sponsor for House Bill 13-1024 during committee hearings, we considered a potential purpose for

this deduction: to clarify that recipients of grants from the Fund are not required to pay Colorado income tax on their grants.

During the House Finance Committee discussion on House Bill 13-1024, the bill sponsor stated, “There is currently no clear guidance from the Internal Revenue Service as to whether grants such as those issued by the Colorado Military Family Relief Fund are required to be included in federal adjusted gross income. The Department of Revenue (Department) is currently treating these grants and labeling them as nontaxable gifts...Given the lack of guidance from the IRS and since it’s unknown whether grantees are currently reporting the grant as income for federal or state tax filings, we’re just seeking to provide clarification by placing in statute that recipients can adjust their federal taxable income when computing their state income tax, thus making monies received by the fund tax exempt.”

We reached out to the Department to confirm that this had been their policy, and Department staff stated that were not aware of any Department policy or practice of treating the grants as nontaxable income. However, both Department staff, and sponsors of the deduction in 2013, noted that it is unclear whether the grants are included in federal taxable income, and by extension, Colorado taxable income. Therefore, by creating this deduction, the General Assembly clarified the tax treatment of grants from the Fund in statute, allowing such grants to be deducted from Colorado taxable income to the extent that a taxpayer had included it in their federal taxable income.

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

We could not definitively determine whether the Military Family Relief Fund Grants Deduction is meeting its purpose because no purpose is provided for it in statute. Additionally, we were unable to determine whether the Deduction is meeting the potential purpose we considered, to clarify that Colorado income tax does not need to be paid on grants

from the Fund, because we lacked data necessary to determine whether eligible taxpayers have used the deduction.

Statute does not provide quantifiable performance measures for this deduction. Therefore, we created and applied the following performance measure to determine the extent to which the deduction is meeting its potential purpose:

*PERFORMANCE MEASURE: To what extent do recipients of grants from the Fund use the deduction to avoid paying income tax on their grants?*

**RESULT:** As a result of this deduction, there is no instance in which a Fund recipient should be paying Colorado income tax on their grant; however, because there is no dedicated line for this deduction on income tax returns, the Department was unable to provide data necessary to determine the extent to which Fund recipients are aware of and using the deduction. We contacted staff from the Colorado National Guard Foundation, and learned that recipients of their grants are not furnished with any information on the tax treatment of their grants. Therefore, we are unable to determine whether recipients of grants from the Fund are aware of the deduction and have excluded any grants they have received from their taxable income.

Additionally, although the federal tax treatment of grants from the Fund is unclear, if grant recipients exclude the grants from their income when filing their federal tax returns, they would not need to use the deduction at the state level. Specifically, since federal taxable income is the starting point for determining Colorado taxable income, if a recipient excludes their grant from their federal taxable income, it would also automatically be excluded from their Colorado taxable income. This would potentially render the state-level deduction, which only allows a deduction to the extent the grant is included in federal taxable income, redundant. After consulting with the Department and conducting our own review of federal tax law, we did not identify any federal law, regulation, or guidance published by the Internal Revenue Service that specifically addresses the federal taxability of grants from

the Fund. However, it is possible that the grants may be excludable from federal adjusted gross income if they are treated as nontaxable gifts under 26 USC 102, although we did not identify any law, regulation, or guidance confirming that this is the correct tax treatment for grants such as those from the Fund. Because ambiguity exists in the federal tax treatment of these grants, we concluded that the Fund's recipients may or may not be including their grants in their federal taxable income, but we lacked data to determine the extent to which this has occurred. Since the grants' exclusion in federal taxable income is likely not uniform, the deduction appears necessary to ensure that all grants from the Fund can be excluded from Colorado taxable income, regardless of whether they were included in federal taxable income.

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

We found that the deduction had a maximum revenue impact to the State of \$9,775 in 2021 and provided a corresponding benefit to taxpayers. Although we lacked data necessary to determine how many taxpayers claimed the deduction, there were 61 grant recipients who were granted a total of \$217,222 in 2021, according to data provided by the Department of Military and Veterans Affairs. Therefore, we multiplied this amount by the State's 4.5 percent income tax rate for 2021 to determine the maximum revenue impact if all of the recipients deducted the full value of the grants from their Colorado taxable income. However, the amount attributable to Colorado's deduction is likely less, to the extent that taxpayers excluded their grants from federal taxable income and were unable to use the state-level deduction or were unaware of the deduction and did not claim it. The revenue impact to the State would have been the same regardless of whether a taxpayer excluded the grant from their federal income or deducted it at the state level. Exhibit 1 shows the total funds granted and the maximum revenue impact of this expenditure in 2019 through 2021, assuming that all recipients of grants from the Fund included their grants in their federal taxable income and used the deduction.

EXHIBIT 1. MAXIMUM REVENUE IMPACT FROM DEDUCTION			
Year	Total Funds Granted	Colorado Income Tax Rate	Maximum Revenue Impact from Deduction
2019	\$172,067	4.63%	\$7,967
2020	\$187,904	4.55%	\$8,550
2021	\$217,222	4.50%	\$9,775
Average	\$192,398	4.56%	\$8,764

SOURCE: Colorado Department of Military and Veterans Affairs, March 2022

### WHAT IMPACT WOULD ELIMINATING THE TAX EXPENDITURE HAVE ON BENEFICIARIES?

If the deduction was repealed, recipients of grants from the Fund who use the deduction to reduce their Colorado taxable income would see an increase in their tax liability, which could reduce the after-tax value of their grant awards. In 2021, based on the average value of grants from the Fund, we estimate that taxpayers who used the deduction reduced their tax liability by about \$160 on average. As discussed, grant recipients who exclude their grants from federal taxable income do not have a need to use the deduction and would not see an impact if it was repealed. Additionally, Fund administrators informed us that, effective February 2022, the maximum benefit from the Fund has been reduced to \$200 per month. Therefore, we anticipate that in future years recipients will receive lower grant amounts from the Fund, and the potential benefit provided by the deduction will decrease commensurately.

Exhibit 2 demonstrates the potential benefit the deduction could have provided to a recipient that received the average grant amount in the 3 most recent years, which would no longer be available if the deduction was repealed.

**EXHIBIT 2. AVERAGE POTENTIAL RECIPIENT  
BENEFIT FROM DEDUCTION**

Year	Number of Grants	Average Annual Grant Amount	Colorado Income Tax Rate	Average Potential Benefit Provided by Deduction
2019	56	\$3,073	4.63%	\$142
2020	64	\$2,936	4.55%	\$134
2021	61	\$3,561	4.50%	\$160

SOURCE: Office of the State Auditor analysis of Colorado Department of Military and Veterans Affairs data.

**ARE THERE SIMILAR TAX EXPENDITURES IN OTHER STATES?**

We did not identify similar tax expenditures in other states.

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

In addition to administering the Fund, the Colorado National Guard Foundation administers the Emergency Assistance Fund, which provides grants to service members who are in need of emergency financial assistance due to hardships, such as medical emergencies, late pay, loss of residence through man-made or natural disaster, death, or other family crises. However, there is not a tax expenditure to create an explicit deduction for recipients of Emergency Assistance Fund grants.

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

We were unable to verify whether recipients of grants from the Fund were using the deduction because there is not a line on the Colorado income tax return specifically for this deduction, and Colorado income tax returns do not show whether taxpayers included their grants in federal taxable income. In order to determine the extent to which the deduction is used and more precisely measure its revenue impact, the



Department would need to create a separate reporting line on the individual income tax return and perform the necessary programming to allow GenTax, its tax information and reporting system, to capture and report this information. According to the Department, these types of changes would require additional resources (see the Tax Expenditures Overview section of the *Office of the State Auditor's Tax Expenditures Compilation Report* for additional details on the limitations of Department data and the potential costs of addressing the limitations). However, based on the small number of grant recipients and relatively small potential revenue impact of the deduction, making these changes may not be cost-effective.

#### WHAT POLICY CONSIDERATIONS DID THE EVALUATION IDENTIFY?

THE GENERAL ASSEMBLY MAY WANT TO CONSIDER AMENDING STATUTE TO ESTABLISH A STATUTORY PURPOSE AND PERFORMANCE MEASURES FOR THE MILITARY FAMILY RELIEF FUND GRANTS DEDUCTION. As discussed, statute and the enacting legislation for the deduction do not state the deduction's purpose or provide performance measures for evaluating its effectiveness. Therefore, for the purposes of our evaluation, we considered a potential purpose for the deduction: to clarify that recipients of grants from the Fund are not required to pay Colorado income tax on their grants. We identified this purpose based on the deduction's operation and testimony from hearings for the enacting legislation (House Bill 13-1024). We also developed a performance measure to assess the extent to which the deduction is meeting this potential purpose. However, the General Assembly may want to clarify its intent for the deduction by providing a purpose statement and corresponding performance measure(s) in statute. This would eliminate potential uncertainty regarding the deduction's purpose and allow our office to more definitively assess the extent to which the deduction is accomplishing its intended goal(s).