STATE OF COLORADO

DEPARTMENT OF REVENUE
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Bill Ritter, Jr.
Governor

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Executive Director

October 26, 2010

The Honorable Brandon Shaffer
President of the Senate
Colorado General Assembly

The Honorable Terrance Carroll
Speaker of the House
Colorado General Assembly

The Honorable John Morse
Senate Majority Leader
Colorado General Assembly

The Honorable Paul Weissmann
House Majority Leader
Colorado General Assembly

The Honorable Mike Kopp
Senate Minority Leader
Colorado General Assembly

The Honorable Mike May
House Minority Leader
Colorado General Assembly

Dear Senators and Representatives:

Nine bills enacted from the 2010 legislative session require the Department of Revenue to account for, on a quarterly and cumulative basis, all revenue that is attributable to their enactment, to the extent such information is available. These bills are HB10-1189, HB10-1190, HB10-1191, HB10-1192, HB10-1193, HB10-1194, HB10-1195, HB10-1196 and HB10-1199.

The data available to the Department is not adequate to reliably and accurately account for all revenue attributable to the enactment of the nine bills mentioned above. This is because the information provided by vendors on sales tax returns does not delineate sales to the level of detail that would be needed to isolate the impact of the implementation of the bills. For the Department to report this information, retailers would have to provide detailed information with regard to sales taxes collected for specific items.

In light of these limitations, the Department has attempted to report information that at least meets the spirit of the requirement by tracking the additional sales tax collected by selected industries assumed to be affected by the enactment of HB10-1189, HB10-1190, HB10-1191, HB10-1192, HB10-1194 and HB10-1195, based on industry code classifications. While this data may include changes that are a direct result of the above mentioned legislation, there are several other factors that affect the sales tax revenue collections by the selected industries such as:

- Changes in the economy (e.g. business cycles, employment variables, inflation, new businesses)
- Previously passed legislation that became effective during this reporting period
- Regulatory changes
- Inability to identify and isolate all businesses that may have been impacted
- Commodity price changes
- Sales within particular industry code classifications may include taxable items that are not specific to the legislation

Furthermore, additional collections due to implementation of the 2010 legislation are not captured exclusively through sales tax collections. Use tax payments by businesses have been affected by the legislation, as well. Businesses or individuals pay use tax primarily if they purchase goods outside of the state for use in the state when the out-of-state vendor does not charge sales tax. For instance, the sales/use tax liability for purchases of computer software from out-of-state vendors would be submitted by Colorado businesses on use tax returns when sales taxes are not collected by the out-of-state vendor. Given that software is purchased by many different types of businesses, the Department cannot isolate the impact of increased use taxes due to the repeal of the sales/use tax exemption on computer software by focusing on use tax collections from specific industry codes. It should be noted that use tax collections for second quarter CY 2010 were $8.6 million greater (a 40.4 percent increase) than use tax collections for the same time period last year. However, given that use tax revenues dipped to low levels during 2009 due to the recession, the increase is most likely due to many reasons including changes/growth in the economy as well as changes in legislation.

An example of how the factors listed above interplay and result in an inability to determine the increase in sales tax revenues attributable to the enacted legislation is provided in the following explanation. HB10-1191 eliminated the sales and use tax exemption on the sales of soft drinks and candy. There is no data on sales tax returns that can account for sales taxes collected specifically for soft drinks and candy. Therefore, the Department can only identify businesses by industry code that may have been affected by the legislation. The targeted industry codes of businesses affected by this legislation include grocery stores, convenience stores, and warehouse clubs. However, these businesses sell many other items in addition to soft drinks and candy, whose prices may increase or decrease or whose popularity may increase or decrease taxable sales. Therefore, although the Department can report the increase in sales taxes collected by businesses in the targeted industry codes, some change in revenues are attributable to factors that affect the sales of other taxable items sold by these businesses. Another factor adding to the uncertainty is that there may be other types of businesses that sell candy or soft drinks that are not included in the targeted list (e.g. pizza delivery businesses that sell liter bottles of soft drinks or craft stores that sell candy). Another factor is the passage of HB09-1342 which eliminated the sales tax exemption for cigarettes, requiring cigarettes to be taxed beginning June 30, 2009. The additional tax collected on the sales of cigarettes would also be a contributing factor in a sales tax revenue increase noted for these same businesses.

As illustrated in the example and because of the factors listed above, it is impossible for the Department to determine the additional revenue that is attributable directly to the enacted legislation.

However, as indicated above, the Department has identified the industry codes that are most likely to distinguish businesses affected by six of the house bills and is providing the following table that indicates the net change in state sales tax revenues collected by the targeted industries, comparing collections in the second quarter of CY 2009 to those in second quarter of CY 2010. The cumulative amount is the total increase in sales taxes collected by the targeted industries when comparing quarterly sales tax collections to the previous year's quarterly sales tax collections, starting with the second quarter of CY 2010. The cumulative amount of sales tax collections for this first report is equal to the quarterly comparison. However, the cumulative amount will increase with each report.

Net Change in Sales Tax Collections from Industries Affected by Sales Tax Budgetary Measures
in Thousands of Dollars*

Bill	Title	2nd Quarter, CY 2010 Net Change**	Cumulative Net Change
HB10-1189	Direct Mail	$93	$93
HB10-1190	Industrial Energy	3,522	3,522
HB10-1191	Candy and Soft Drinks	5,506	5,506
HB10-1192	Software Regulation	1,237	1,237
HB10-1194	Food Containers	142	142
HB10-1195	Agricultural Products	1,288	1,288

* Please see Appendix A for industry code classifications used above to estimate net change in sales tax collections
** Net change is compared to 2nd Quarter, CY 2009.

The table does not include revenues associated with the passage of HB10-1193, HB10-1196 and HB10-1199 for the following reasons:

- HB10-1193 specifies that as of March 1, 2010, all out-of-state retailers that conduct business in Colorado are required to collect state sales tax on items purchased by Colorado purchasers. Otherwise, the retailer is required to notify Colorado purchasers that use tax is due on certain purchases and that the state of Colorado requires the purchaser to file a use tax return. These notifications are to occur by January 31st, following the calendar year in which the purchases were made and requires payment of the tax by April 15th following the calendar year in which the purchases were made. The Department can report the increase in total use taxes paid. The first report would compare second quarter CY 2011 collections to second quarter CY 2010 collections; however, some of the potential documented increase could be due to other factors, similar to the increase in collections associated with the other bills as businesses pay use tax for the purchase of equipment from out-of-state businesses. Additionally, the state may realize an increase in sales tax collections attributable to this bill if the internet retailers choose to collect sales taxes for Colorado purchases; however, taxable internet purchases by Colorado residents are not specific to any one or even a few industry codes; therefore, the Department cannot isolate a change in sales tax revenues as it relates to this legislation.

- HB10-1196 establishes a $6,000 limit on the amount of income tax credit allowed for certain vehicles that are fuel efficient (category 7 vehicles) purchased on or after January 1, 2010 but before January 1, 2011 and eliminates the credit, thereafter. The revenue change created by this legislation will not be available until income tax year 2011 returns are submitted to the Department. The Department will begin receiving these returns after January 1, 2012 and will document this information in its report to legislative leadership for the first quarter of CY 2012.

- HB10-1199 establishes a temporary cap of $250,000 on the net operating loss that may be claimed by a company. This cap is in place for income tax years 2011, 2012 and 2013. Net operating loss may be carried forward one additional year for each tax year that a company is prohibited from claiming additional net operating loss. The Department will be unable to report the revenue impact of this legislation because the amount of a deduction carried forward by a corporation is not separately tracked by the Department's accounting system (although this information is available on a case-by-case basis to auditors by manually reviewing a submitted return).

Please contact Mark Couch at the Department of Revenue, with any questions that you may have. Mark may be reached at 303-866-2819 or mcouch@spike.dor.state.co.us.

Sincerely,

Roxy Huber

Roxy Huber
Executive Director
Colorado Department of Revenue

BILL #	Brief Description	Impacted Industries Code Classifications
HB10-1189	Direct Mail	▪ Direct Mail Advertising
HB10-1190	Industrial Energy	▪ Electric Power Generation, Transmission and Distribution ▪ Natural Gas Distribution ▪ Water, Sewage and Other Systems
HB10-1191	Candy and Soft Drinks	▪ Supermarkets and Other Grocery (except Convenience) Stores ▪ Convenience Stores ▪ Confectionary and Nut Stores ▪ Pharmacies and Drug Stores (except Medical Marijuana Dispensaries) ▪ Food (Health) Supplement Stores ▪ Warehouse Clubs and Supercenters
HB10-1192	Software Regulation	▪ Computer and Computer Peripheral Equipment and Software Merchant Wholesalers ▪ Computer and Software Stores ▪ Software Publishers
HB10-1194	Food Containers	▪ Service Establishment Equipment and Supplies Merchant Wholesalers ▪ Industrial and Personal Service Paper Merchant Wholesalers ▪ General Line Grocery Merchant Wholesalers
HB10-1195	Agricultural Products	▪ Crop Production ▪ Animal Production ▪ Support Activities for Agriculture and Forestry ▪ Other Farm Product Raw Material Merchant Wholesalers ▪ Restricted Use Pesticide Dealers