



TABOR REFUND MECHANISMS

by Kate Watkins

This issue brief provides information on the TABOR refund mechanisms under current law.

Article X, Section 20 of the Colorado Constitution requires that revenue in excess of the Taxpayer's Bill of Rights (TABOR) limit be refunded to taxpayers. The General Assembly may statutorily determine how this "surplus" revenue is refunded. Over the course of TABOR's history, there have been 21 different refund mechanisms. However, under current law there are three: the six-tier sales tax refund, the Earned Income Tax Credit (EITC) refund mechanism, and the temporary income tax rate reduction. Each of these mechanisms is described in greater detail in this issue brief.

To date, there have been six years when the state experienced a TABOR surplus, the most recent of which occurred during FY 2004-05. In total, Colorado taxpayers received nearly \$3.3 billion in refunds from the six surplus years. Referendum C, which was passed by the voters in the November 2005 general election, allowed the state to retain and spend all surplus revenue above the TABOR limit for a period of five years from FY 2005-06 through FY 2009-10. Therefore, no refunds were available during this time.

From FY 2010-11 through at least FY 2013-14, state revenue forecasts do not anticipate any TABOR refunds as revenue is not expected to exceed the TABOR limit.

Description of the TABOR Refund Mechanisms

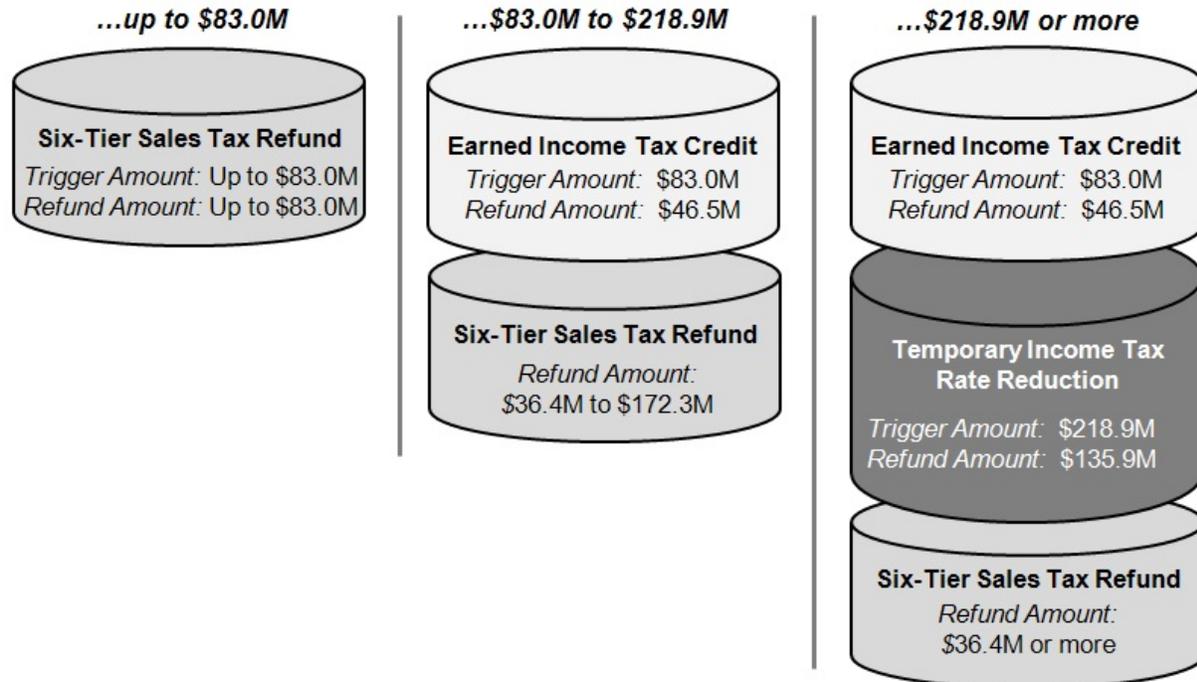
Six-tier sales tax refund. This refund mechanism allows individuals to receive a state sales tax refund based on six modified federal adjusted gross income tiers and the filing status of the taxpayer. The Department of Revenue sets the dollar amount of each tier and each tier's refund based on set percentages of the refund and number of taxpayers in each tier. The refund is distributed to the six tiers when the TABOR surplus is large enough to support at least a \$15 refund for each Colorado taxpayer. For instance, in FY 2010-11 this threshold is an estimated \$44.9 million. In the event of a surplus that is less than the \$15 per taxpayer trigger, an equal refund would be provided to each taxpayer regardless of income.

In terms of prioritization, the six-tier sales tax refund mechanism can be viewed as both the first and the last refund mechanism. It may be the first and only refund triggered in a year when the surplus is not sufficient to trigger other mechanisms. This was the case in FY 2004-05. In years when the surplus is large enough to trigger other refund mechanisms, the six-tier sales tax refund mechanism refunds any surplus revenue remaining after the other refunds.

Figure 1, on the following page, shows how the TABOR surplus would be refunded under current law based on the size of the surplus. All dollar amounts are estimates for FY 2010-11 based on the September 2010 Legislative Council Staff forecast.

Figure 1. TABOR Surplus Refund Scenarios Under Current Law

*If, in FY 2010-11, the TABOR Surplus was...**



Source: Dollar amounts are based on the September 2010 Legislative Council Staff forecast for FY 2010-11.

**This figure is for illustrative purposes. No TABOR surplus is projected for FY 2010-11.*

Earned Income Tax Credit (EITC) refund mechanism. The Colorado EITC "piggybacks" off of the federal EITC, which provides a tax credit to individuals who work but do not earn high incomes. Qualifying Colorado taxpayers may receive up to 10 percent of the federal credit amount in TABOR surplus years. Only Colorado taxpayers who claim the federal credit may claim the state credit. For tax years 2009 and 2010, the federal American Recovery and Reinvestment Act (ARRA) expanded the EITC. To qualify for the EITC in these tax years, earned income and adjusted gross income for individuals must each be less than:

- \$43,279 (\$48,279 married filing jointly) with three or more qualifying children;
- \$40,295 (\$45,295 married filing jointly) with two qualifying children;
- \$35,463 (\$40,463 married filing jointly) with one qualifying child; and
- \$13,440 (\$18,440 married filing jointly) with no qualifying children.

The EITC refund mechanism is triggered when the surplus exceeds a threshold amount which is increased by a growth factor equal to Colorado personal income growth each year.

Temporary income tax rate reduction. This refund mechanism will first become available for TABOR surplus years starting in FY 2010-11. Under the refund mechanism, the state income tax rate would be temporarily reduced from the current rate of 4.63 percent to 4.50 percent. The rate reduction will occur in the tax year following the fiscal year in which there is a surplus. For example, if there were a surplus in FY 2010-11, the income tax rate would be temporarily reduced in tax year 2011.

The temporary income tax rate reduction is triggered when the state experiences a surplus equal to at least the EITC refund mechanism trigger plus the projected amount of the income tax rate reduction. As Figure 1 shows, this amount is projected to be \$218.9 million for FY 2010-11 (a \$135.9 million tax rate reduction plus the \$83.0 million EITC threshold).