Legislative Council Staff
Nonpartisan Services for Colorado's Legislature

Room 029 State Capitol, Denver, CO 80203-1784
Phone: (303) 866-3521 • Fax: (303) 866-3855
lcs.ga@state.co.us • leg.colorado.gov/lcs

Memorandum

January 31, 2022

TO: Joint Budget Committee

FROM: Kate Watkins, Chief Economist, 303-866-3446

SUBJECT: CY 2021 ARPA Revenue Loss

Summary

Among the allowable uses of federal American Rescue Plan Act (ARPA) funds, states have the most flexibility in spending the portion of funding used to offset the state revenue loss attributable to the COVID-19 pandemic. This memorandum provides information on the revenue loss reported for calendar year (CY) 2020 and the preliminary loss calculated for CY 2021, estimated at $1.14 billion and $2.55 billion, respectively. The preliminary cumulative two-year revenue loss is $3.69 billion, compared with the $3.83 billion total ARPA allocation for the state of Colorado. Additional revenue losses are possible in CY 2022 and CY 2023.

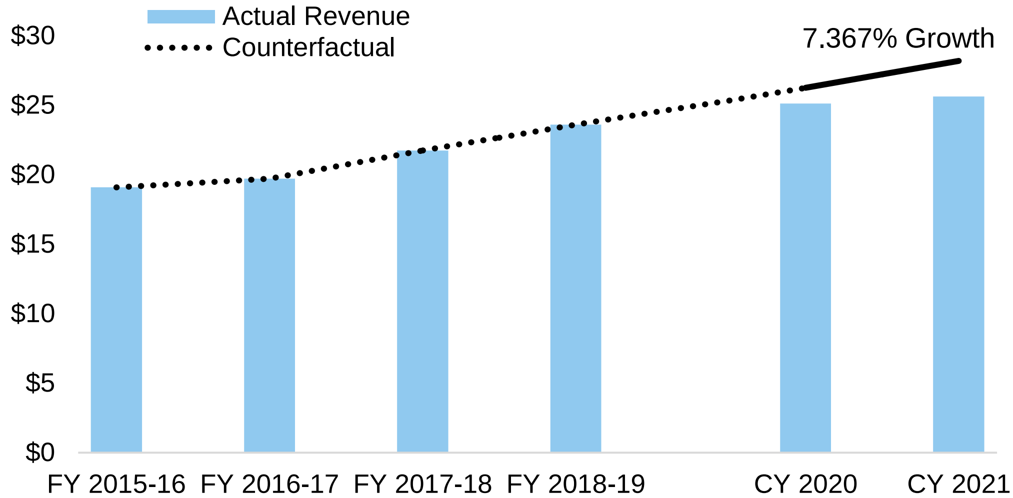
Revenue Loss Methodology

Guidance issued by the U.S. Department of Treasury provides a methodology for how to calculate state revenue losses. These losses are based on the difference between actual state "general revenue from own sources"" and a "counterfactual," an alternative amount intended to approximate revenue that would have been collected if not for the pandemic. "General revenue" includes all General Funds and most cash funds. This includes about $10 billion more than what is included in the quarterly revenue forecasts for revenue subject to TABOR, and includes revenue streams such as higher education tuition and fees.

The counterfactual is calculated based on average annual growth in state general revenue between FY 2015-16 and FY 2018-19 (which is 7.367 percent for the state of Colorado). The counterfactual is grown from FY 2018-19 revenue amounts and compared to actual collections on a calendar year basis. The difference between actual revenue and the counterfactual is calculated at four points in time: calendar years 2020, 2021, 2022, and 2023.[1] Figure 1 provides a visual representation of actual general revenue and the counterfactual for the state of Colorado through CY 2022.

[1] For additional details and information on the U.S. Treasury guidance under the final rule, see: https://home.treasury.gov/system/files/136/SLFRF-Final-Rule.pdf

Figure 1
Colorado Actual "General Revenue" vs. the ARPA Counterfactual
Dollars in Billions



Source: Data provided by the Office of the State Controller. p = Preliminary.

How does Colorado's calculation address the TABOR limit? Colorado's methodology for calculating the revenue loss effectively treats TABOR as if it does not exist. In other words, revenue is treated as if it is not limited by the Referendum C cap.

How does Colorado's calculation address accruals? U.S. Treasury guidance allows states to apply the revenue loss calculation on either a calendar year or fiscal year basis, though initial guidance only allowed a calendar year calculation. Colorado's revenue loss is based on a calendar year calculation. There are benefits to using the calendar year calculation, in that it provides information on the revenue loss six months ahead of the fiscal year calculation, and may result in a larger revenue loss..

Consistent with state accounting practices, revenue is moved into the fiscal year in which the underlying economic activity occurs. This is done through an "accrual adjustment" at the end of the fiscal year. For example, sales tax collections are typically remitted a month after a sale takes place. Each year, accrual adjustments are made to shift July collections back into the prior fiscal year.

In order to estimate calendar year revenue, fiscal year accruals were included in the calendar year ending the fiscal year (e.g., FY 2019-20 accruals are applied to CY 2020).

CY 2020 Revenue Loss Update

In May 2021, preliminary calculations based on available data suggested a $1.3 billion revenue loss for CY 2020.[2] As the Office of the State Controller (OSC) has finalized financial reporting for FY 2020-

[2] The $1.3 billion amount was reported in the Legislative Council Staff memorandum dated May 20, 2021, available at: https://leg.colorado.gov/sites/default/files/r21-994_legislative_changes_and_flexibility_in_use_of_american_rescue_plan_funds.pdf

21 in conjunction with the release of the Comprehensive Annual Financial Report (CAFR), this amount has changed slightly to $1.14 billion. The $1.14 billion amount has been officially reported to the U.S. Treasury.[3]

Preliminary CY 2021 Revenue Loss

With the close of calendar year 2021, preliminary state revenue collections suggest a $2.55 billion revenue loss. This additional revenue loss may be surprising considering strong growth in General Fund collections and the TABOR surplus situation in FY 2020-21 and expected in FY 2021-22. That said, the nuances of the ARPA revenue loss calculation result in different pools of revenue and different time periods than forecast revenue subject to TABOR. The following provides additional context for the CY 2021 revenue loss.

Large income tax accrual adjustments boosted CY 2020 revenue and reduced CY 2021 revenue. Delayed income tax filing deadlines resulted in large accrual adjustments over the past two fiscal years. In 2020, instead of the usual April income tax filing deadlines, filing deadlines were pushed to July (into the next fiscal year). As a result, FY 2019-20 income tax accrual adjustments were very large (more than $1.0 billion) because they pulled the delayed income tax filings from FY 2020-21 back into FY 2019-20. For the purposes of the ARPA revenue loss calculation, the large positive FY 2019-20 accrual was added to the monthly collections for the twelve months of CY 2020, thus boosting the revenue amount in that calendar year and reducing the revenue loss.

FY 2020-21 accrual adjustments were also very large but in the opposition direction (-$1.1 billion) because what was accrued into FY 2019-20 was pulled out of FY 2020-21. When this large negative FY 2020-21 accrual was combined with the twelve months of collections for CY 2021, it resulted in a calendar year-over-year decline in income tax revenue. This was one of the largest factors contributing to the revenue loss in CY 2021.

Slower growth in some revenue streams. The other primary reason for the additional revenue loss is that some other revenue streams grew at a slower pace than the counterfactual. In particular, higher education tuition and fees, which make up about 11 percent of general revenue, were basically flat (up only 0.1 percent above prior calendar-year levels). These slow growth revenue streams, coupled with the decline year-over-year in the income tax streams due to the accrual adjustments, slowed total revenue growth. Total general revenue grew at a pace of 2.1 percent year-over-year in CY 2021, compared to the 7.367 percent counterfactual.

[3] For additional information on the amounts reported, see the Office of the State Controller memorandum to the Joint Budget Committee, dated January 31, 2022.