



## Fiscal Note

### Legislative Council Staff

Nonpartisan Services for Colorado's Legislature

## HB 26-1223: MODIFYING CERTAIN TAX EXPENDITURES

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**Prime Sponsors:**

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Sen. Ball; Roberts

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**Fiscal note status:** This fiscal note reflects the reengrossed bill.

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### Summary Information

**Overview.** The bill narrows the downloadable software sales and use tax exemption and creates an expanded family affordability credit.

**Types of impacts.** The bill is projected to affect the following areas on a continuous basis:

- State Expenditures
- State Revenue
- Local Government

**Appropriations.** No appropriation is required.

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**Table 1**  
**State Fiscal Impacts**

Type of Impact	Budget Year FY 2026-27	Out Year FY 2027-28
State Revenue	\$0	\$0
State Expenditures	\$0	\$8,778
Transferred Funds	\$0	\$0
Change in TABOR Refunds	\$0	\$0
Change in State FTE	0.0 FTE	0.0 FTE

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The bill has offsetting positive and negative impacts on state revenue. See Table 1A and State Revenue section.

**Table 1A  
 State Revenue**

<b>Fund Source</b>	<b>Budget Year FY 2026-27</b>	<b>Out Year FY 2027-28</b>
General Fund from Software Exemption	\$44.4 million	\$92.2 million
General Fund from Family Affordability Credit	-\$44.4 million	-\$92.2 million
Cash Funds	Minimal	Minimal
<b>Total Revenue</b>	<b>\$0</b>	<b>\$0</b>

**Table 1B  
 State Expenditures**

<b>Fund Source</b>	<b>Budget Year FY 2026-27</b>	<b>Out Year FY 2027-28</b>
General Fund	\$0	\$8,778
Cash Funds	\$0	\$0
Federal Funds	\$0	\$0
Centrally Appropriated	\$0	\$0
<b>Total Expenditures</b>	<b>\$0</b>	<b>\$8,778</b>
<b>Total FTE</b>	<b>0.0 FTE</b>	<b>0.0 FTE</b>

## Summary of Legislation

The bill modifies the state sales and use tax base and creates a new income tax credit.

### Downloadable Software Exemption

The bill narrows the downloadable software sales and use tax exemption so that only custom software developed for use by a particular user and software governed by a negotiable license agreement is exempt from taxation. Under the bill, all other types of downloadable software are subject to state sales and use tax beginning January 1, 2027. The bill states that its changes to the sales tax base do not automatically apply to the sales tax base used by the Regional Transportation District (RTD) and the Scientific and Cultural Facilities District (SCFD), which otherwise use the state sales tax base.

Beginning January 1, 2027, the bill additionally decreases the percent of sales tax revenue diverted to the Housing Development Grant Fund (HDGF) from 1.655 percent to 1.625 percent of sales tax revenue.

## **Expanded Family Affordability Credit**

Starting for tax year 2027, the bill creates an expanded family affordability credit (EFAC) for Coloradans who are or would be eligible for the Family Affordability Tax (FATC) available in current law. The credit is refundable, meaning any amount by which the credit exceeds a taxpayer's tax liability is refunded to the taxpayer.

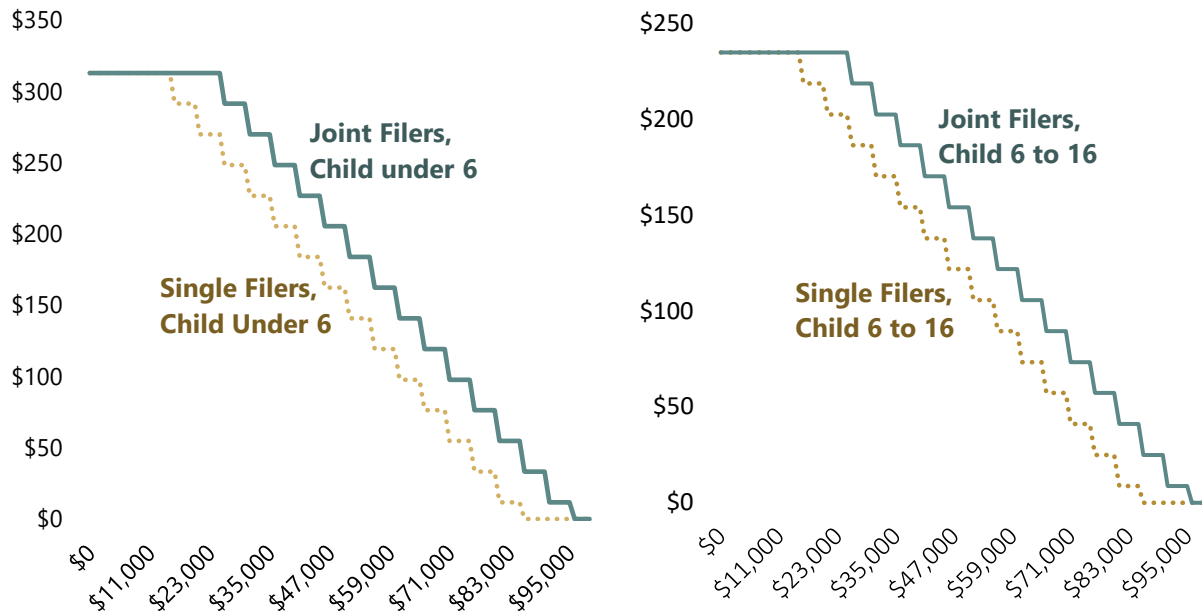
The amount of the EFAC depends on the estimated amount of the state revenue increase that results from the sales tax exemption change in the bill. Starting with the December 2027 forecast Legislative Council Staff is required to determine the maximum dollar amounts of the EFAC so that the projected aggregate total of tax credits claimed is equal to the net amount of revenue gain attributable to the narrowing of the software sales tax exemption.

Based on this fiscal note's estimates of the revenue increase from the change to the downloadable software exemption, the projected amount of the EFAC in tax year 2027 is:

- For each child under age 6, \$313 for single filers with AGI of \$16,000 or less, reduced by \$22 (6.875 percent) for every \$5,000 of AGI above \$16,000; and
- for each child ages 6 to 16, \$235 for single filers with AGI of \$16,000 or less (75 percent of the credit for children under age 6), reduced by \$16 (6.875 percent) for every \$5,000 of AGI above \$16,000; or
- for each child under age 6, \$313 for joint filers with AGI of \$27,000 or less, reduced by \$22 (6.875 percent) for every \$5,000 of AGI above \$26,000; and
- for each child ages 6 to 16, \$235 for joint filers with AGI or \$27,000 or less (75 percent of the credit for children under age 6), reduced by \$16 (6.875 percent) for every \$5,000 of AGI above \$26,000.

Figure 1 shows the amount of credit allowed in tax year 2027 for taxpayers for each eligible child, depending on their AGI and the child's age. Starting with tax year 2028, credit amounts and AGI amounts are adjusted for inflation.

**Figure 1**  
**HB 26-1223 Tax Credit Amounts by Adjusted Gross Income, Filing Status, and Child's Age**  
**Tax Year 2027**



## Background

### Family Affordability Tax Credit

Enacted by [House Bill 24-1311](#), the FATC is a refundable income tax credit available to Coloradans with children under age 17 and a federal adjusted gross income (AGI) in 2024 up to \$85,000 for single filers and up to \$95,000 for joint filers. Credit amounts and AGI are adjusted annually for inflation. The amounts and availability of the credit are dependent on state revenue conditions. For tax year 2024, approximately 320,490 Coloradans claimed the FATC for a total of \$865.9 million in income tax credits. The credit is available in full for tax year 2025 and unavailable for tax year 2026. Under the March 2026 LCS forecast, the FATC is expected to be unavailable in tax years 2027 and 2028.

### Downloadable Software Exemption

Under current law, only software that is prepackaged via a tangible physical medium is subject to the state sales and use tax. Examples of software that are exempt from sales and use tax include:

- software that is used over the internet without being downloaded to the user's computer, such as with "cloud computing";

- software downloaded from the internet to the customer's computer or other electronic device;
- software that is manually installed on a consumer's computer or electronic device by a vendor's representative; and
- custom software developed for use by a particular user.

In 2024, the amount of sales and use tax exemptions reported under the downloadable software exemption totaled \$15.3 million across 47,762 sales tax returns. However, it is probable that some software-as-a-service (SaaS) retailers reported software exemptions under the service exemption rather than the downloadable software exemption, such that the amount of sales reported under the downloadable software exemption is an underestimate of sales that would become subject to sales and use tax under this bill.

## Assumptions

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According to the U.S. Census Bureau, there were \$11.89 billion prepackaged software sales in 2022 in Colorado, up from the \$5.10 billion posted for 2017. Based on that data, it is estimated that there will be \$16.44 billion in Colorado software sales in FY 2026-27, and \$17.67 billion in FY 2027-28, with increasing amounts in future years. The fiscal note assumes that 90 percent of software is downloadable. Since businesses are assumed to account for a significant portion of software sales and software companies likely negotiate contracts with businesses, it is assumed that 20 percent of total downloadable software sales arise from nonnegotiable agreements and would become subject to state sales tax. Because of data constraints, this fiscal note contains high, bidirectional uncertainty. Different estimation methodologies and assumptions produce significantly different estimates. To the extent that more or less software sales are downloadable and nonnegotiable than assumed in the fiscal note, actual revenue increases will respectively be higher or lower than the fiscal note estimate.

## **State Revenue**

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Because the bill requires total funding availability for the tax credit to depend on projected sales and use tax revenue attributable to the exemption modifications under this bill, the bill is estimated to have a net \$0 impact on state revenue.

### **Downloadable Software Sales Tax Exemption**

The narrowing of the software sales and use tax exemption combined with the decrease in percent of sales tax revenue allocated to the HDGF is expected to increase General Fund revenue subject to TABOR by \$44.4 million in FY 2026-27 (half-year impact), and \$92.2 million in FY 2027-28 with increasing amounts in future years.

While sales tax revenue is distributed to the General Fund and the HDGF, the increase in HDGF revenue as a result of the software exemption changes is expected to be offset by the decrease in HDGF revenue from decreasing the percent of sales tax revenue allocated to the HDGF from 1.655 to 1.625. This results in minimal change to expected of sales tax revenue allocated to the HDGF.

### **Expanded Family Affordability Credit**

The EFAC will decrease General Fund revenue subject to TABOR by \$44.4 million in FY 2026-27, and \$92.2 million in FY 2027-28, with increasing amounts in future years.

## **State Expenditures**

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The bill increases state expenditures in the Department of Revenue (DOR) by \$8,778 in FY 2027-28, and \$8,702 in FY 2028-29 and future years. These costs, paid from the General Fund, are for data management and reporting.

Expenditures in the Office of Research and Analysis are required for changes in the related GenTax reports so that the department can access and document tax statistics related to the new tax policy. These costs represent 231 hours in FY 2027-28 and 229 hours in FY 2028-29 and future years for data management and reporting at \$38 per hour.

## **TABOR Refunds**

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While the bill impacts state revenue streams subject to TABOR, the net revenue impact to the state is \$0. As a result, the bill has no impact to the state's TABOR refund obligation.

## **Local Government**

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The bill will increase sales and use tax revenue for the state-collected local governments that incorporate the exemption and conform to the state tax base. Special districts and state-collected city and county governments are allowed to modify the exemption in their sales tax base, but are not required to do so.

## **Effective Date**

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The bill takes effect upon signature of the Governor, or upon becoming law without his signature. The modification of the downloadable software sales and use tax exemption is effective January 1, 2027.

## **State and Local Government Contacts**

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Counties	Revenue
Local Affairs	Special District Association
Municipalities	State Auditor
Regional Transportation District	Personnel

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The revenue and expenditure impacts in this fiscal note represent changes from current law under the bill for each fiscal year. For additional information about fiscal notes, please visit the [General Assembly website](#).