INSTITUTE ON TAXATION AND ECONOMIC POLICY

Economic Modeling on Colorado Tax Reallocation Measure

The Institute on Taxation and Economic Policy (ITEP) is a non-profit, non-partisan research organization that provides timely, in-depth analyses on the effects of federal, state, and local tax policies. ITEP has conducted analysis of the proposed policy using a microsimulation tax model and this memo summarizes these findings.

There are insufficient data available for ITEP to estimate the precise cost of the credit for all newly eligible populations--particularly students and for caregivers of dependents who are age 70+ or are disabled. However, for the eligible participants ITEP was able to model, we estimate a cost of $1.413 billion assuming 2018 tax law and incomes with 57% of Colorado resident tax returns receiving the credit. (While the first taxable year in which the credit would be claimed is 2019, we assume an estimate based in 2018 incomes and tax law provides an accurate estimate of total potential cost since changes in the cost of the credit from 2018 to 2019 will be small due to minor inflation adjustments to the federal EITC on which part of the credit is based.)

For the modeled population, this cost estimate reflects full participation in order to ensure the proposed increase in the personal income taxes fully covers the cost of the new credit. The credit is anticipated to have higher uptake than the state's current EITC because of the higher value of the credit, monthly distribution of the credit in recipients' bank accounts, and because a larger percentage of recipients are middle income people who would otherwise owe taxes and will be filing anyway.

In analyzing the personal income tax scenarios, ITEP finds that the 11.8% tax on taxable income in excess of $500,000 would raise $1.376 billion in tax year 2018, which when added to the projected $81 million cost of the current Colorado EITC, provides a total of $1.457 billion to fund the credit. ITEP estimates that 0.9% of Colorado resident tax returns would be affected by the new tax bracket.

ITEP further finds that the 9.87% tax on taxable income in excess of $300,000 would raise $1.400 billion, which when added to the projected $81 million cost of the current Colorado EITC provides a total of $1.481 billion to fund the credit. ITEP estimates that 2% of Colorado resident tax returns would be affected by the new tax bracket.

ITEP anticipates that in both scenarios, the revenue yields will be higher in 2019.

Thus, ITEP concludes that the revenue increase from the additional income tax rate/bracket would be sufficient to fund the revenue reduction from the expanded EITC and that the overall measure is revenue neutral.

About the ITEP Microsimulation Tax Model Overview

The ITEP Microsimulation Tax Model, developed in 1996, is a tool for calculating revenue yield and incidence, by income group, of federal, state and local taxes. The ITEP model is capable of calculating the impact of current tax law and tax change proposals on taxpayers and can also project potential revenue yields of tax law changes. The model is unique in its ability to produce analysis at the federal and state levels and to analyze income, consumption and property based taxes.

In computing its estimates, the ITEP model relies on one of the largest databases of tax returns and supplementary data in existence, encompassing close to three quarters of a million records. To forecast revenues and incidence, the model relies on government or other widely respected economic projections.

The ITEP model's federal tax calculations are very similar to those produced by the congressional Joint Committee on Taxation, the U.S. Treasury Department and the Congressional Budget Office (although each of these four models differs in varying degrees as to how the results are presented). The ITEP model, however, adds state-by-state estimating capabilities not found in those government models.

Data Sources
As "microsimulation model," the ITEP model works on a very large stratified sample of tax returns and other data, aged to the year being analyzed. The ITEP model uses the following micro-data sets and aggregate data:

> **Micro-Data Sets**
> IRS 1988 Individual Public Use Tax File, Level III Sample; IRS Individual Public Use Tax Files; Current Population Survey; Consumer Expenditure Survey; U.S. Census; American Community Survey.
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> **Partial List of Aggregated Data Sources**
> Miscellaneous IRS data; Congressional Budget Office and Joint Committee on Taxation forecasts; other economic data (Moody's Economy.com, Commerce Department, WEFA); state tax department data; data on overall levels of consumption for specific goods (Commerce Department, Census of Services); state specific consumption and consumption tax data (Census data, Government Finances, data from state revenue departments); state specific property tax data (Govt. Finances, data from state revenue departments.); American Housing Survey; Census of Population Housing; and other sources.

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