



Legislative Council Staff

Nonpartisan Services for Colorado's Legislature

Demographic Note

Drafting Number:	LLS 21-0476	Date:	May 31, 2021
Prime Sponsors:	Rep. Sirota; Weissman Sen. Hansen; Moreno	Analyst:	Elizabeth Ramey 303-866-3522 Elizabeth.Ramey@state.co.us

BILL TOPIC: **INCOME TAX**

Demographics Analyzed: • Socioeconomic Status • Race/Ethnicity

Direct Impact(s): Economic Health Public Safety
 Employment Education

Bill Impact: This bill increases after-tax income for certain lower-income households that qualify for new and expanded income tax credits, and reduces after-tax income for certain higher-income households eligible for income tax deductions repealed by the bill. In doing so, the bill may decrease existing disparities in economic outcomes, including disparities by socioeconomic status, race, and ethnicity.

Report Status: This demographic note reflects the reengrossed bill.

Demographic Impact Summary

This demographic note¹ analyzes potential impacts of HB 21-1311 on disparities in economic outcomes based on available data, including by socioeconomic status as measured by income, race, and ethnicity.² The bill makes various changes to Colorado income tax policy, including reducing taxable income deductions and creating new and expanded income tax credits. The bill may reduce disparities by increasing after-tax income for lower-income households claiming the new state Child Tax Credit and expanded state Earned Income Tax Credit (EITC), and by reducing after-tax income for higher-income households claiming deductions for contributions to 529 accounts, capital gains deductions, itemized deductions, deductions for business meals, and qualified business income deductions. These changes may reduce economic disparities by socioeconomic status, race, and ethnicity.

¹Pursuant to Section 2-2-322.5, C.R.S., this demographic note uses available data to outline the potential impacts of proposed legislation on disparities within the state. Disparities are defined by statute as the difference in economic, employment, health, education, or public safety outcomes between the state population as a whole and subgroups of the population, as defined by socioeconomic status, race, ethnicity, sex, gender identity, sexual orientation, disability, geography, or any other relevant characteristic for which data are available. It is beyond the scope of this analysis to examine each of the varied causes contributing to a given disparity. For further information on the contents of demographic notes, see "Demographic Notes Overview" Memorandum available at https://leg.colorado.gov/sites/default/files/images/lcs/demographic_notes_overview.pdf.

² Terminology used to distinguish demographic groups (e.g., black/African American, Hispanic or Latina/Latino) is based on the terminology used in the data sources referenced. These terms may differ from the self-identification of these populations.

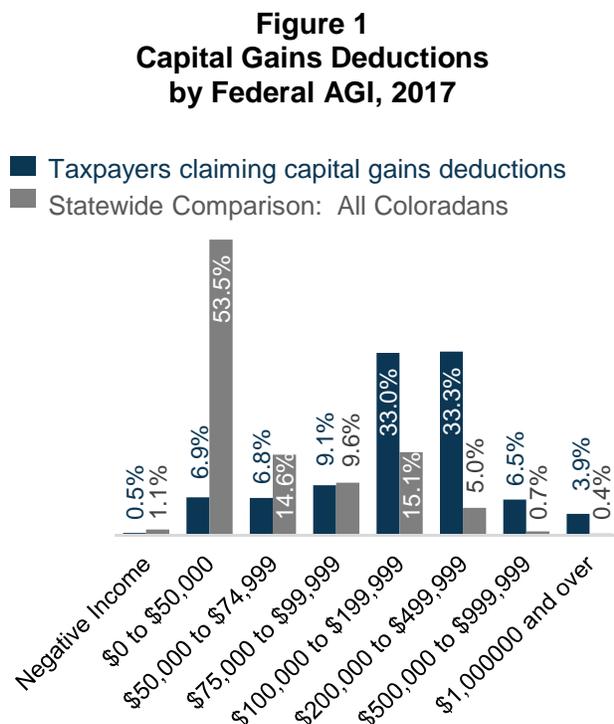
Demographic characteristics of Colorado households by income suggest that lower-income black/African American, Hispanic, and other/multiracial individuals are more likely to experience after-tax income increases as a result of the bill and higher-income white, Asian, and non-Hispanic individuals are more likely to incur after-tax income reductions via an increase in tax liability under HB 21-1311. To the extent that the bill alters taxpayer behavior, there may be additional impacts potentially offsetting those identified in this demographic note.

Key Provisions and Demographic Comparisons

For each of the major provisions of the bill, the following analysis presents the demographic considerations raised by the bill and, where data are available, compares the populations affected by the bill to the statewide population across different demographic groups. Pursuant to statute and based on available data on demographic differences between affected and statewide comparison populations, this analysis identifies potential effects of the bill on existing disparities. For more detailed information on the data used, see Appendix A.

Provisions that May Increase Tax Liability for Certain Taxpayers

Capital gains. The bill repeals the state income tax deduction for certain federally taxable capital gains after tax year 2021. Based on data from the 2020 Colorado Tax Profile and Expenditure Report, this deduction is primarily claimed by individual income tax filers. Among these filers, 76.7 percent of deductions were claimed by taxpayers with an adjusted gross income of \$100,000 and over (Figure 1). Other demographic data are not available for taxpayers claiming the deduction.

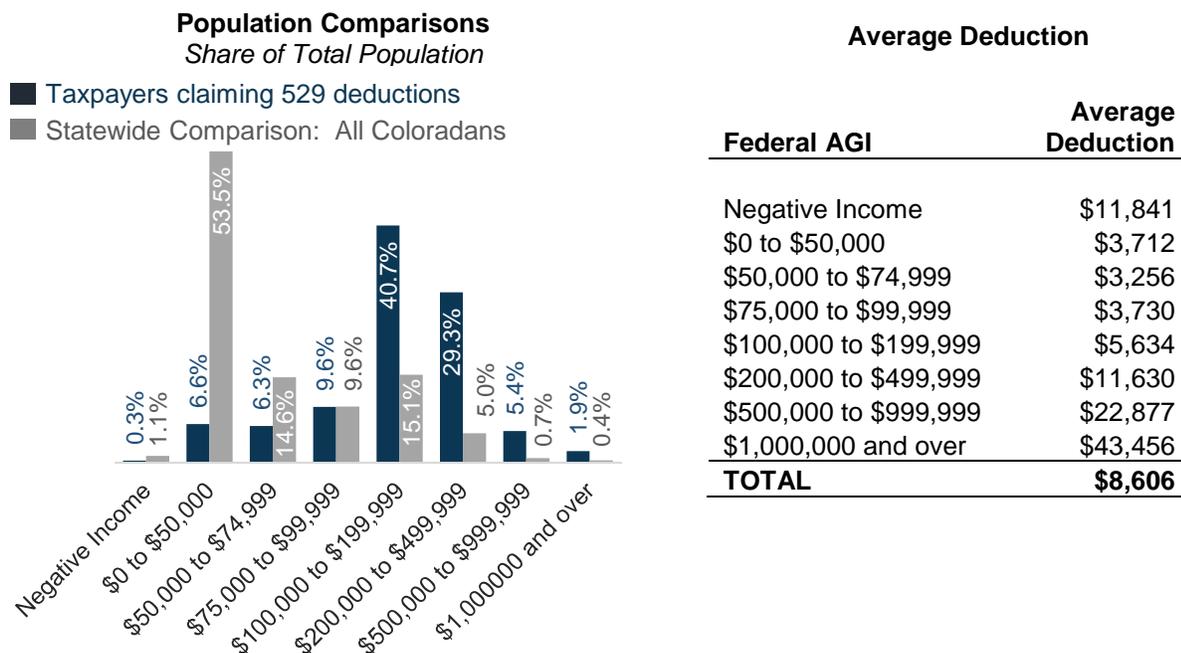


Source: Colorado Department of Revenue, “2020 Colorado Tax Profile and Expenditure Report.”

Contributions to a 529 account. Under current law, taxpayers may deduct the amount they contribute to a CollegeInvest 529 account from their Colorado taxable income. Beginning in the 2022 tax year, the bill limits this deduction to \$15,000. In 2019, 9,400 taxpayers made contributions exceeding these limits.

The left panel of Figure 2 shows the income distribution, as measured by federal adjusted gross income (AGI), of 529 deduction claimants compared to that of all Colorado income taxpayers. More than half of all taxpayers have an income between \$0 and \$50,000, compared to just 6.6 percent of those claiming 529 deductions. A majority of claimants of 529 deductions fall into income groups above \$100,000. As shown in the right panel of Figure 2, higher income groups (\$500,000 and above) also have average deduction amounts that exceed the maximum threshold in the bill. Other demographic data was not available for taxpayers claiming this deduction.

Figure 2
Colorado Tuition Program (529) Deductions by Federal AGI, 2017



Source: Colorado Department of Revenue, "2020 Colorado Tax Profile and Expenditure Report."

Business meal deduction. The bill requires taxpayers to add back half of the federal deduction for business meals when calculating Colorado taxable income for 2022 only. The demographic impacts of the add-back for the meal expense deduction is indeterminate as demographic data could not be identified for those claiming or benefiting from the deduction. Based on available federal income tax data for nonfarm sole proprietors in tax year 2016, sole proprietors with higher net income tend to claim a larger share of businesses expense deductions, including but not limited to meal expenses.³

Qualified business income deduction. The bill extends the requirement that certain taxpayers add back their federal qualified business income when calculating their Colorado taxable income through tax year 2025. The add-back applies to high income taxpayers with AGI over \$500,000 for those filing singly and \$1,000,000 for those filing jointly.

Itemized deductions. Beginning in tax year 2022, the bill requires taxpayers with adjusted gross incomes (AGI) of \$400,000 or more to add back a portion of their federal itemized deductions when calculating their Colorado taxable income.

Corporate and insurance company income tax modifications. The demographics of those impacted by the bill's corporate income tax modifications could not be determined. The bill changes how corporate income among a combined group of affiliated corporations is apportioned to Colorado. It also prevents corporations from using tax shelters in foreign jurisdictions for the purpose of tax avoidance. The bill also makes certain insurance companies subject to the state income tax rather than the insurance premium tax. These provisions of the bill are expected to increase tax costs for affected businesses while increasing state tax revenue.

³ IRS Statistics of Income, Nonfarm Sole Proprietorship Statistics, Table 3: Number of Returns, Business Receipts, Business Deductions, Net Income, by Industry and Size of Business Receipts, Tax Year 2016. Available at: <https://www.irs.gov/statistics/soi-tax-stats-nonfarm-sole-proprietorship-statistics>

The population affected by these provisions of the bill cannot be determined, as impacts are dependent on business and government decisions that are unknown. For example, corporations may pass any increased tax costs onto their customers, incur reduced profits, or pursue other response strategies.

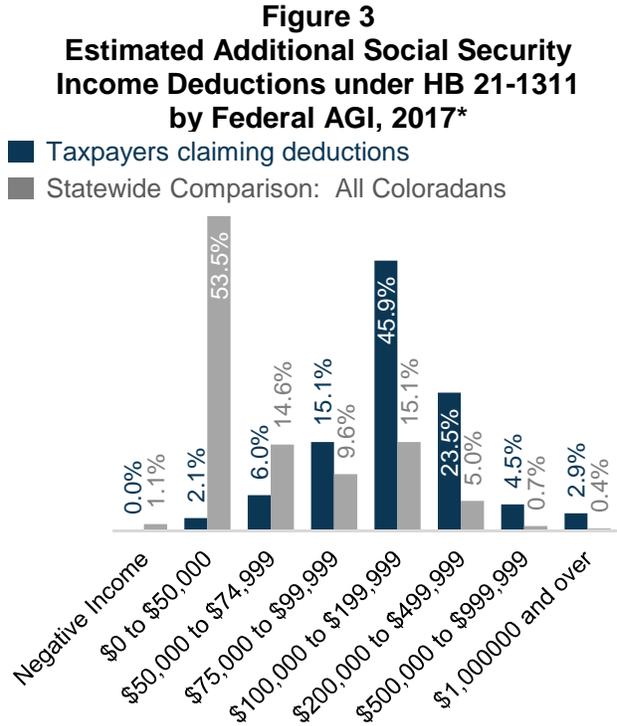
Provisions that May Decrease Tax Liability for Certain Taxpayers

Social security income. Under current law, taxpayers may deduct a limited amount of pension and annuity income, including social security income, when calculating their Colorado taxable income. The bill removes the cap on pension and annuity income deductions for federally taxable social security income so that all federally taxed social security income is deductible in Colorado. The deduction is limited to taxpayers 55 and over.

Based on Colorado Department of Revenue estimates, this provision of the bill is expected to benefit mainly higher-earning taxpayers, with 76.8 percent of those likely to claim the deduction having adjusted gross income of \$100,000 and over compared to 21.2 percent of all taxpayers (Figure 3). Other demographic data was not available for taxpayers claiming this deduction.

Earned income tax credit. Colorado taxpayers who claim the federal EITC or who would otherwise be able to claim the federal EITC but are ineligible because they do not have a social security number may claim the Colorado EITC.

This is a refundable credit calculated as a percentage of the federal credit. For tax year 2022, the bill increases the state EITC from 15 percent to 20 percent of the federal EITC; for 2023 through 2025, the state EITC is increased to 25 percent of the federal EITC. The federal EITC is available to taxpayers below a certain income level ranging from almost \$16,000 for a single filer with no children to a maximum of almost \$60,000 for married filers with three or more children. As shown in Table 1, over 99 percent of claimants of the state EITC have AGI of \$50,000 or below.



Source: Colorado Department of Revenue.
 * Estimates for deductions under the bill are based on 2018 preliminary Colorado statistics of income.

Table 1
State EITC Tax Credits by Federal AGI, 2017

	Population	Share of Total
Negative Income	2,922	0.9%
\$0 to \$9,999	76,743	24.5%
\$10,000 to \$19,999	95,364	30.5%
\$20,000 to \$29,999	61,119	19.5%
\$30,000 to \$39,999	53,925	17.2%
\$40,000 to \$49,999	20,424	6.5%
\$50,000 to \$59,999	2,185	0.7%
\$60,000 to \$74,999*	21	0.0%
\$75,000 to \$99,999*	11	0.0%
TOTAL	312,714	100.0%

Source: Colorado Department of Revenue.

* Credits to these taxpayers reflect a mismatch between reported AGI on federal and state tax returns.

Business conversion income tax credit.

The bill creates a temporary income tax credit equal to 50 percent of the conversion costs for a business that converts to a worker-owned cooperative, an employee stock ownership plan (ESOP), or an employee ownership trust. The maximum amount of the income tax credit is up to \$25,000 when converting to a worker-owned cooperative or an employee ownership trust, and up to \$100,000 when converting to an employee stock ownership plan. The most recent available data indicate that there are 131 businesses with an ESOP and 34 worker-owned cooperatives in Colorado. There is no data on existing employee ownership trusts as this is a relatively new type of business form.

To the extent that the tax credit incentivizes shifts to greater employee ownership than what would have occurred under current law, business income may be more evenly distributed across employees than would occur under current law. While only limited data are available on the impacts of employee ownership, a 2017 study using survey data from the National Longitudinal Surveys found for those between ages 28 and 34, employees working for employee-owned businesses tended to have higher median wages, higher household wealth, and were more likely to have access to employee-based health insurance, tuition reimbursement, and other benefits.⁴ These employees were also more likely

Child tax credit. The bill makes a state refundable child tax credit available to taxpayers beginning in tax year 2022. The credit is available for single income tax filers with less than \$75,000, and for joint filers with less than \$85,000 in federal adjusted gross income, provided they claimed either the federal child tax credit or the additional child tax credit, regardless of the federal requirement that a qualifying child must have a social security number. Credit amounts are adjusted for income levels, with those in lower income groups eligible to claim a higher percentage of the federal credit, ranging between 10 and 60 percent. Estimated filers by federal AGI are shown in Table 2.

Table 2
Estimated State Child Tax Credits by Federal AGI, 2018*

Single Filers	Population	Share of Total
\$25,000 or less	39,807	25.8%
\$25,001 to \$50,000	31,832	20.6%
\$50,000 to \$74,999	9,096	5.9%
Joint Filers		
\$35,000 or less	19,561	12.7%
\$35,001 to \$60,000	26,896	17.4%
\$60,001 to \$85,000	27,017	17.5%
TOTAL	154,209	100.0%

Source: Colorado Department of Revenue.

* Estimates for credit claimed under the bill are based on 2018 preliminary Colorado statistics of income.

⁴ Wiefek, Nancy. 2007. "Employee Ownership & Economic Well-Being: Household Wealth, Job Stability, and Employment Quality among Employee-Owners Age 28 to 34." Published by the National Center for Employee Ownership. Available at: https://www.ownershipconomy.org/wp-content/uploads/2017/05/employee_ownership_and_economic_wellbeing_2017.pdf

to remain at their place of work longer. Data could not be identified for age groups above the 28 to 34 range.

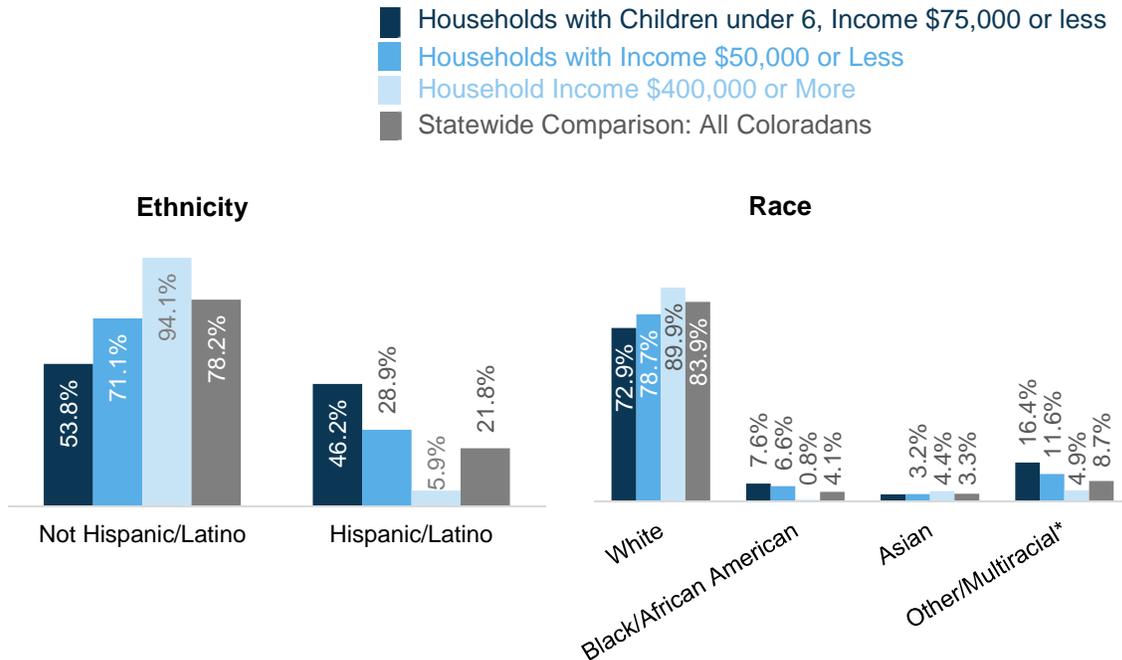
Demographics of Colorado Households by Income

Income is often correlated with other demographic characteristics, as shown in Figure 4, which compares the racial and ethnic composition of selected affected populations, including:

- households with children under six and incomes of \$75,000 or less (the populations eligible for the child tax credit);
- households with income of \$50,000 or less (those eligible for the EITC);
- households with income of \$400,000 or more (higher income earners who are more likely to claim many of the deductions that are repealed under the bill); and
- the statewide population as a whole (comparison population).

The data suggest that Coloradans living in lower income households with and without children under six are more likely to be Hispanic and black/African American, multiracial, or of another race, while those living in higher income households are more likely to be non-Hispanic and white or Asian.

Figure 4
Population Comparisons
Share of Total Population



Source: U.S. Census Bureau, American Community Survey 1-Year Estimates, 2019.

* Other races include American Indian, Alaska Native, Native Hawaiian, other Pacific Islander, or some other race alone.

Analysis and Findings

The bill is expected to increase after-tax income for lower-income households claiming the new state child tax credit and expanded state EITC, to increase after-tax income for higher-income taxpayers aged 55 and over claiming expanded social security income deductions, and to reduce after-tax

income for higher-income taxpayers claiming reduced deductions for contributions to 529 accounts, capital gains deductions, itemized deductions, deductions for business meals, and qualified business income deductions. The bill is expected to benefit businesses and their employees converting to a worker-owned cooperative, an employee ownership trust, or an employee stock ownership plan. Finally, the bill is expected to reduce business income for certain corporations and insurance companies. To the extent that the bill alters taxpayer behavior, there may be additional, potentially offsetting impacts that cannot be known at this time.

Based on a comparison between the statewide and affected populations, this analysis suggests that the bill may reduce existing economic disparities by socioeconomic status, race, and ethnicity. Demographic characteristics of Colorado households by income suggest that individuals living in lower-income households affected by the bill are more likely than the statewide population to be black or African American, multiracial or of another race, and Hispanic and higher-income households affected by the bill are more likely to be white or Asian and non-Hispanic.

Disparities in context. While HB 21-1311 reduces income disparities for many low-income households, it is unlikely to influence other factors that contribute to income or other disparities. It is important to note that economic disparities such as those discussed here have multiple and interacting causes, including not only individual behavior and choices, but also historical and structural factors that can shape or constrain individual choices and distribute economic and other opportunities unevenly to individuals on the basis of their membership in particular demographic groups.

Demographics Not Analyzed

Some demographic groups have not been included in the analysis due to data limitations. Data on the relevant populations delineated by sex, gender identity, disability, sexual orientation, and geography were not available at the time of the analysis. Should data become available, this analysis may be updated.

Data Sources and Agencies Contacted

Revenue

Economic Development and International Trade

**Appendix A
Population Data Used in Analysis**

Colorado Tuition Program (529) Deductions by Federal AGI, 2017

Income	Taxpayers Claiming Deductions			Statewide Comparison: All Taxpayers	
	Population	Share of Total	Average Deduction	Population	Share of Total
Negative Income	159	0.3%	\$11,841	26,648	1.1%
\$0 to \$50,000	3,662	6.6%	\$3,712	1,300,480	53.5%
\$50,000 to \$74,999	3,484	6.3%	\$3,256	355,684	14.6%
\$75,000 to \$99,999	5,307	9.6%	\$3,730	232,845	9.6%
\$100,000 to \$199,999	22,633	40.7%	\$5,634	366,150	15.1%
\$200,000 to \$499,999	16,261	29.3%	\$11,630	122,007	5.0%
\$500,000 to \$999,999	2,984	5.4%	\$22,877	18,107	0.7%
\$1,000,000 and over	1,075	1.9%	\$43,456	8,653	0.4%
TOTAL	55,565	100.0%	\$8,606	2,430,574	100.0%

Source: Colorado Department of Revenue.

Capital Gains Deductions by Federal AGI, 2017

Income	Taxpayers Claiming Deductions		Statewide Comparison: All Taxpayers	
	Population	Share of Total	Population	Share of Total
Negative Income	28	0.5%	26,648	1.1%
\$0 to \$50,000	412	6.9%	1,300,480	53.5%
\$50,000 to \$74,999	406	6.8%	355,684	14.6%
\$75,000 to \$99,999	545	9.1%	232,845	9.6%
\$100,000 to \$199,999	1,976	33.0%	366,150	15.1%
\$200,000 to \$499,999	1,990	33.3%	122,007	5.0%
\$500,000 to \$999,999	389	6.5%	18,107	0.7%
\$1,000,000 and over	236	3.9%	8,653	0.4%
TOTAL	5,982	100.0%	2,430,574	100.0%

Source: Colorado Department of Revenue.

Estimated Additional Social Security Income Deductions by Federal AGI, 2017*

Income	Taxpayers Expected to Claim Increased Deductions			Statewide Comparison: All Taxpayers	
	Population	Share of Total	Average Deduction	Population	Share of Total
Negative Income	NR	0.0%	\$0	26,648	1.1%
\$0 to \$50,000	570	2.1%	\$3,625	1,300,480	53.5%
\$50,000 to \$74,999	1,641	6.0%	\$3,462	355,684	14.6%
\$75,000 to \$99,999	4,098	15.1%	\$3,493	232,845	9.6%
\$100,000 to \$199,999	12,476	45.9%	\$4,156	366,150	15.1%
\$200,000 to \$499,999	6,373	23.5%	\$5,256	122,007	5.0%
\$500,000 to \$999,999	1,214	4.5%	\$5,819	18,107	0.7%
\$1,000,000 and over	798	2.9%	\$6,010	8,653	0.4%
TOTAL	27,170	100.0%	\$4,390	2,430,574	100.0%

Source: Colorado Department of Revenue. NR = Not reportable due to taxpayer confidentiality requirements.

* Estimates for deductions under the bill are based on 2018 preliminary Colorado statistics of income.

Colorado Households by Income and Race, 2019

Race	Households with Children under 6, Income \$75,000 or less		Households with Income \$50,000 or Less		Household Income \$400,000 or More		All Households	
	Population	Share of Total	Population	Share of Total	Population	Share of Total	Population	Share of Total
White	351,722	72.9%	1,086,779	78.7%	144,582	89.9%	4,830,882	83.9%
Black/ African American	36,848	7.6%	90,467	6.6%	1,293	0.8%	236,390	4.1%
Asian	14,851	3.1%	43,669	3.2%	7,124	4.4%	189,867	3.3%
Other/Multiracial*	78,980	16.4%	159,604	11.6%	7,814	4.9%	501,597	8.7%
TOTAL	482,401	100.0%	1,380,519	100.0%	160,813	100.0%	5,758,736	100.0%

Source: U.S. Census Bureau, American Community Survey 1-Year Estimates, 2019.* Other races include American Indian, Alaska Native, Native Hawaiian, other Pacific Islander, or some other race alone.

Colorado Households by Income and Ethnicity, 2019

Ethnicity	Households with Children under 6, Income \$75,000 or Less		Households with Income \$50,000 or Less		Household Income \$400,000 or More		All Households	
	Population	Share of Total	Population	Share of Total	Population	Share of Total	Population	Share of Total
Not Hispanic/Latino	259,440	53.8%	981,326	71.1%	151,387	94.1%	4,501,783	78.2%
Hispanic/Latino	222,961	46.2%	399,193	28.9%	9,426	5.9%	1,256,953	21.8%
TOTAL	482,401	100.0%	1,380,519	100.0%	160,813	100.0%	5,758,736	100.0%

Source: U.S. Census Bureau, American Community Survey 1-Year Estimates, 2019.