Deloitte.

Deloitte Tax LLP | June 29, 2021

MULTISTATE TAX

Colorado enacts several law changes impacting income and indirect taxes

Tax Alert

Overview

On June 23, 2021, Colorado Governor Jared Polis signed into law Colorado House Bills 21-1311 and 21-1312 (HB 1311 and HB 1312), which provide for several changes to Colorado's corporate and individual income taxes as well as indirect taxes.

This Tax Alert provides a summary of some of the more significant provisions in the bills.

Summary of corporate income tax changes

- HB 1311 modifies Colorado's computation of the receipts factor for apportionment of combined corporations to require that all corporations in the combined group with any Colorado receipts must utilize the "Finnigan method" to determine the Colorado receipts in the numerator for tax years beginning on or after January 1, 2022. Colorado currently uses the "Joyce method."

- HB 1311 modifies the definition of an "affiliated group" to "includable C corporations connected directly or indirectly through stock ownership." The requirement that the common parent be an includable C corporation remains in place.

- For tax years beginning on or after January 1, 2022, HB 1311 requires that the Colorado combined group include C corporations "incorporated in a foreign jurisdiction for the purpose of tax avoidance." The legislation includes a rebuttable presumption that a corporation is created for tax avoidance purposes if it is incorporated in one of 44 listed jurisdictions and includes information on how to calculate the taxable income of a foreign corporation that is to be included in the Colorado combined group.

- HB 1311 disallows the Internal Revenue Code (IRC) section 78 dividend subtraction from any foreign corporations created for tax avoidance purposes that are included in a Colorado combined return.

- HB 1311 creates a subtraction for any net GILTI (global intangible low-taxed income) or IRC section 951 income of a foreign corporation created for tax avoidance purposes that is included in a Colorado combined return.

- HB 1311 provides that for tax years beginning on or after January 1, 2022, corporations are required to addback any federal deductions for food and beverage under IRC section 274(n)(2)(D) that exceed 50% of the total expense.

- HB 1311 provides that for tax years beginning on or after January 1, 2022, the qualified Colorado capital gain exclusion is limited to taxpayers with farming activity reported on federal Schedule F with qualified capital gains.

- HB 1311 creates a tax credit for businesses that create an Employee Stock Ownership Plan ("ESOP") or an Employee Ownership Trust or that convert to a Worker-Owned Cooperative. The credit amount is based on defined "conversion costs" and the plan must be approved by the state.

- HB 1311 makes captive insurance companies taxable entities for Colorado corporate income tax purposes if 50% or less of the entities' receipts are from premiums for insurance arrangements.

Summary of individual income tax changes

- HB 1311 extends the Colorado limitation on the amount of IRC section 199A deductions that are allowed for certain high-income taxpayers for an additional three years. This provision is effective for tax years beginning on or after January 1, 2021, but before January 1, 2026.

- HB 1311 creates a limit on federal itemized deductions that are allowed for Colorado purposes for taxpayers with federal adjusted gross income of $400,000 or more. Effective for tax years beginning on or after January 1, 2022, the limit is set at $30,000 for taxpayers filing a single return and $60,000 for taxpayers filing a joint return.

- For tax years beginning on or after January 1, 2022, but before January 1, 2023, HB 1311 requires taxpayers to add back any federal deductions claimed of more than 50% of food and beverage expenses.

- HB 1311 increases the cap on the deduction for federally taxed pension annuity benefits for tax years beginning on or after January 1, 2022, for certain taxpayers who are 65 or older to include all federally taxed social security benefits.

- HB 1311 limits deductions for contributions to 529 Plans for tax years beginning on or after January 1, 2022 to $20,000 per beneficiary (adjusted for inflation) for taxpayers filing a single return and $30,000 per beneficiary (adjusted for inflation) for taxpayers filing a joint return.

- HB 1311 increases the Colorado earned income tax credit for Colorado residents to 20% of the federal credit claimed for tax years beginning on or after January 1, 2022, but before January 1, 2023. For tax years beginning on or after January 1, 2023, but before January 1, 2026, the Colorado earned income tax credit increases to 25% of the federal credit claimed. The state credit reverts to 20% of the federal credit claimed for tax years beginning on or after January 1, 2026.

- HB 1311 makes the Colorado child tax credit available for tax years beginning on or after January 1, 2022, based on a percentage of the federal tax credit that varies by the amount of the taxpayer's federal adjusted gross income.

- HB 1311 provides that for tax years beginning on or after January 1, 2022, the qualified Colorado capital gain exclusion is limited to taxpayers with farming activity reported on federal Schedule F with qualified capital gains.

Summary of sales and use tax changes

- HB 1312 includes digital goods in the definition of tangible personal property, and defines digital goods as "any item of tangible personal property that is delivered or stored by digital means, including but not limited to video, music, electronic books, or computer files."

- HB 1312 imposes sales tax on amounts charged for mainframe computer access, photocopying, and packing and crating.[1]

- Currently, a retailer who collects sales tax can retain 4% of the state sales tax collected (known as a vendor fee), with a monthly cap of $1,000. Effective January 1, 2022, HB 1312 eliminates the vendor fee for any filing period where the retailer's total taxable sales are greater than $1 million.

Summary of property tax changes

- For purposes of imposing property tax, HB 1312 requires the actual value of real property to reflect the value of the fee simple estate. The bill requires that the actual value of personal property be determined based on the property's value in use, which will be defined by the property tax administrator.

- There is an exemption from property tax for business personal property that is less than a certain amount, which increases with inflation. HB 1312 increases this exemption from $7,700 to $50,000 for tax years beginning on January 1, 2021 and January 1, 2022. For tax years beginning on January 1, 2023, the amount of the exemption will be adjusted biennially by the property tax administrator.

Summary of insurance premium and severance tax changes

- Currently, the insurance premium tax is equal to 2% of premiums collected or contracted for covering property or risk, with an exception that a company that maintains a home office or regional home office in Colorado pays tax at a rate of 1%. HB 1312 requires that a company have at least 2% of its workforce in Colorado to be considered a home or regional home office in calendar year 2022. The amount increases to 2.25% for calendar year 2023 and 2.5% for all subsequent calendar years.

- Also related to insurance premium tax, HB 1312 narrows the tax exemption for annuities considerations to those purchased through a qualified retirement plan, a Roth 401(k), or an individual retirement account.

- With regards to severance taxes, HB 1312 limits the netback deductions to direct costs, which disallows costs of capital and other indirect expenses.

- Currently, the first 300,000 tons of quarterly coal produced is exempt from property tax. Additionally, there is a tax credit of 50% from underground coal production and another credit of 50% for lignite coal. Beginning with the 2022 taxable year, the quarterly exemption and both tax credits related to coal production will be phased out.

Get in touch

Lance Williams
Jeff Maxwell
Mikaela Neumuller

Footnotes

[1] The bill adds to C.R.S. section 39-26-102, subsection 5.7, defining "mainframe computer access" to mean the "provision of access to computer equipment for the purpose of storing or processing data." As well as amending the statute under subsection 6.5, "photocopying" is now defined as the "sale of a document rendered on paper or other similar material by a machine that creates an accurate reproduction of the original." The bill also adds subsection 6.4 to the statute, which defines "packing and crating" to mean "tangible personal property furnished to prepare tangible personal property at retail for delivery to a location designated by the purchaser."