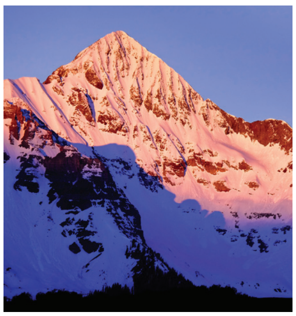
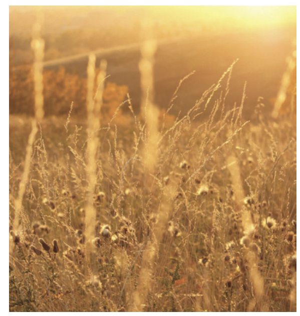
Report on Federal Tax Law Provisions and Changes that Impact the Colorado Tax Base

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OFFICE OF THE STATE AUDITOR

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OFFICE OF THE STATE AUDITOR

KERRI L. HUNTER, CPA, CFE • STATE AUDITOR

June 29, 2026

Members of the Legislative Oversight Committee Concerning Tax Policy, Joint Budget Committee, and House and Senate Finance Committees,

This report contains the results of our study and evaluation of federal tax law and changes at the federal level that may have a significant impact on the State's tax base or otherwise impact taxable income within the state due to the State's policy of using federal taxable income as the basis for Colorado taxable income, as required by Section 39-21-306, C.R.S.

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Report on Federal Tax Law Provisions and Changes that Impact the Colorado Tax Base

Overview

Colorado uses federal taxable income as the starting point for calculating Colorado taxable income and conforms to the current version of the federal Internal Revenue Code [Title 26 of the United States Code (26 USC)] for both corporate and individual taxpayers. This means that Colorado generally conforms with federal policies for determining what is considered income for the purposes of calculating income tax and the amount taxpayers may deduct when calculating taxable income. Additionally, if the federal government amends the Internal Revenue Code (IRC), in most cases the amendments are automatically incorporated into Colorado's income tax base and could potentially impact the amount of income tax revenue that Colorado receives.

House Bill 24-1053 (codified at Section 39-21-306, C.R.S.) requires the State Auditor to annually "study and evaluate impacts to the state's policy of using federal taxable income as the basis for Colorado taxable income. The evaluation must include a review of federal tax law, including changes, that may have a significant impact on the state's tax base or otherwise impact taxable income within the state." This report, the second issued under this requirement, includes:

- A background section, which provides an overview of how federal taxable income is calculated for individual and corporate taxpayers, a brief legislative history of Colorado's income tax base, a comparison of how other states calculate their state income taxes and their conformity to the IRC, and the implications of federal conformity.
- A section outlining the current impact of Colorado using federal taxable income as its tax base.
- A recent and pending changes section, which summarizes changes to federal tax law that occurred since the publication of our most recent federal report in June 2025 through April 2026 that may impact Colorado.
- Several appendices, which are referred to throughout the report to provide more specific information on topics such as what items of income are included in gross income, what items are excluded from income, descriptions of deductions allowed to be taken at the federal level (including data on how frequently they are claimed and the amount, when available) and their impact on the State, Colorado income tax credits that are calculated based on federal credits, and a list of the types of organizations exempt from federal income tax.

- Note for 2026 Federal Report: This report often re-uses IRS statistics of income data that was included in our 2025 report. We were not able to update these figures because new information was not publicly available at the time of publication.

Background

How Does the Calculation of Federal Taxable Income Impact Colorado Taxable Income?

To understand the relationship between federal tax policies and the tax revenue Colorado collects, a basic understanding of how federal and Colorado taxable income are calculated is helpful. As outlined below, taxpayers generally must calculate their federal taxable income, which is the starting point for calculating Colorado taxable income, before they can determine their Colorado tax liability. Additionally, corporate taxpayers are subject to separate laws regarding the calculation of taxable income and tax liability.

Calculating Federal Taxable Income for Individuals

As shown in Exhibit 1, individuals calculate their federal taxable income by first determining what is included in gross income, then subtracting certain deductions known as "above-the-line" deductions to determine federal adjusted gross income. From adjusted gross income, individual taxpayers can claim either the standard deduction, which provides a standard deduction amount based on taxpayers' filing status (e.g., single, married filing jointly), or itemize deductions, which allows taxpayers to take deductions based on certain actual expenses they incurred during the year. A few additional deductions are available for individuals after taking either the standard deduction or itemizing deductions to arrive at federal taxable income.

Exhibit 1
How Federal Taxable Income is Calculated for Individuals

	Federal Gross Income (exclusive of exclusions)
–	"Above-the-Line" Deductions
=	**Federal Adjusted Gross Income**
–	Standard Deduction or Itemized Deductions
–	Qualified Business Deduction
–	Charitable Contribution Deduction for Non-itemizing Taxpayers
–	Personal Exemptions
=	**Federal Taxable Income**

Source: Office of the State Auditor analysis of federal laws.

As will be discussed in more detail in the sections that follow, federal tax laws, regulations, administrative rulings, and court decisions govern how taxpayers may calculate each step of the process shown in Exhibit 1, and ultimately determine how much tax they must pay. For example, the determination of federal gross income is subject to a body of law defining what income is and excluding certain types of income for tax purposes; when taxpayers are allowed to exclude more income from their gross income for tax purposes, they will generally have less taxable income and pay less in taxes. Similarly, the extent to which taxpayers are allowed to subtract deductions from their gross income and adjusted gross income will determine their taxable income and tax liability.

Calculating Federal Taxable Income for Corporations

In many ways, the calculation of corporations' federal taxable income is similar to individuals. For example, corporations share the same definition of gross income for federal tax purposes as individuals: "all income from whatever source derived" [26 USC 61(a)] and may exclude income only as explicitly provided by the IRC. Corporations are also allowed to claim deductions from gross income when calculating their federal taxable income [26 USC 63(a)]. However, computation of federal taxable income for corporations differs from individuals in important ways that impact the types of deductions they typically claim and the calculation of taxable income. Generally, U.S. tax laws for corporations are designed to tax businesses on their net income (i.e., revenues in excess of expenses) and establish when they must recognize revenue, expenses, and income for tax purposes, since the timing of revenues may not match the timing of expenses related to those revenues. This section describes how corporations calculate their federal taxable income, with an emphasis on concepts that are applicable to businesses, such as cost of goods sold, capitalizing versus expensing expenditures, and business-oriented deductions.

Similar to federal income taxes for individuals, federal laws establishing when businesses must recognize sales revenue, costs, and income all impact the calculation of federal taxable income as shown in each step of Exhibit 2. For example, if a business is allowed to exclude certain income in any given tax period, it will generally recognize less federal gross income and pay less in taxes. Similarly, the more losses and other deductions a business can subtract from its gross income, the less it will generally owe in taxes.

Exhibit 2
How Federal Taxable Income is Calculated for Corporations

	Gross Sales
–	Cost of Goods Sold
=	**Federal Gross Income**
–	Deductions
=	**Federal Taxable Income**
–	Federal Net Operating Loss Deduction
–	Special Deductions
=	**Net Federal Taxable Income**

Source: Office of the State Auditor analysis of federal laws.

Cost of goods sold. Cost of goods sold is a concept that is important for businesses that make or sell goods (i.e., producers/manufacturers or resellers/retailers). According to case law [Patients Mutual Assistance Collective Corp. v. Commissioner (2018)], "COGS [cost of goods sold] is the costs of acquiring inventory, through either purchase or production." Cost of goods sold is technically an exclusion from gross income rather than a deduction because it is subtracted from gross sales to calculate gross income. Federal law provides that businesses must recover costs related to the inventories that they produce or acquire for resale in the same tax period that they sell the inventory, rather than take deductions for those expenses in the year in which the expense was incurred. For example, if a company spends $100 on 10 items to resell, it cannot necessarily deduct that $100 in costs related to the acquisition of the goods in the year of the purchase. Rather, the company subtracts those costs from gross sales at the time it sells the inventory. In this example, if the company sells 5 of the items in a year, it may subtract $50 from gross sales to arrive at gross income in that year. Costs directly, and in many cases indirectly, related to the inventory must also be recovered over time (as cost of goods sold). Examples of direct costs include the cost of the items themselves (if a reseller) or raw materials/components of an item as well as labor directly used to manufacture the items (if a producer/manufacturer). Examples of indirect costs include management expenses and materials that are not a part of the final product but are used to produce it. Additionally, the types of costs that must be included in cost of goods sold may vary depending on the type of business.

Depreciation of capital assets. Subject to some exceptions provided in the IRC, expenditures made to acquire or create an asset with a useful life of more than a year, improve property, restore property, or adapt property for a new use cannot be deducted entirely in the current tax year. Instead, these expenditures must be capitalized and recovered through depreciation or amortization over time. According to Bloomberg Law, "The policy underlying the disallowance of current deductions for capital expenditures is that the cost of an asset that remains productive in the taxpayer's business for a period of years should be recovered over the period that the asset provides benefits to the business; therefore, the expenditure does not represent a current operating expense." The IRC provides the recovery periods for broad classes of assets, and in some cases allows for accelerated recovery periods (i.e., shortened depreciation or amortization periods). Generally, depreciation is deducted from federal gross income as part of calculating federal taxable income.

Net operating losses. A net operating loss occurs when a taxpayer's allowable deductions exceed their income for the tax year. In general, a net operating loss means that a taxpayer has "negative income" in a particular tax year and does not have income tax liability in that year. A net operating loss carryback or carryforward allows a taxpayer to subtract their net operating loss from federal taxable income in past or future tax years, respectively. This policy is generally meant to factor in businesses' long-term profits or losses in determining their tax liability, and can ultimately reduce the taxpayer's tax liability across multiple years. A net operating loss carryback, which allows the taxpayer to reduce net taxable income in a prior tax year can result in an immediate refund to the taxpayer, assuming they had filed and paid taxes during the tax year the net operating loss is applied to; whereas, a net operating loss carryforward can be subtracted from income in future tax years resulting in a lower tax liability in those years. A taxpayer may claim a net operating loss deduction for up to 80 percent of their federal taxable income (computed without regard to the net operating loss deduction). Most taxpayers can carry forward net operating losses indefinitely but not carry them back to prior years.

Calculation of tax liability. After corporations have calculated their federal taxable income, they apply the federal tax rate to it to determine their tax liability. The federal corporate income tax is imposed at a flat rate of 21 percent. It is important to note that corporations that have income from business activities both within and outside of Colorado do not typically pay Colorado income tax on their entire federal taxable income. Rather, these corporations apportion and allocate their income among the jurisdictions in which they earn income.

Calculating Colorado Taxable Income

In general, since Colorado uses federal taxable income as the starting point for calculating Colorado taxable income and generally conforms to the current IRC (known as "rolling conformity"), most aspects of federal law that impact the calculation of federal taxable income at the federal level also flow through to Colorado and impact Colorado taxable income, and ultimately state tax revenue, unless the General Assembly enacts legislation to deviate from federal tax treatment. Specifically:

- Any income item that is excluded from federal gross income is also excluded from Colorado taxable income unless the General Assembly enacts legislation to include it, typically through an adjustment to taxable income known as an "addback." Similarly, any deduction that is allowed for federal tax purposes is also incorporated into Colorado taxable income unless the General Assembly enacts legislation to disallow it, typically through an addback.

- Any income that is included in federal gross income is also included in Colorado taxable income unless the General Assembly enacts legislation to exclude it, typically through an adjustment to taxable income known as a "subtraction." Similarly, any deduction that is not allowed for federal tax purposes is not incorporated into Colorado taxable income unless the General Assembly enacts legislation to allow a deduction at the state level, typically through a "subtraction."

Exhibit 3 shows the calculation of Colorado tax liability, using federal taxable income as the starting point.

Exhibit 3
How Colorado Income Tax is Calculated

	Federal Taxable Income
+	State Addbacks
−	State Subtractions
=	**Colorado Taxable Income** x **Colorado Income Tax Rate (4.4 %)**
=	**Colorado Tax Liability**
−	Colorado Credits
=	**Colorado Income Tax Due**

Source: Office of the State Auditor analysis of state tax laws.

Legislative History of Colorado's Income Tax Base

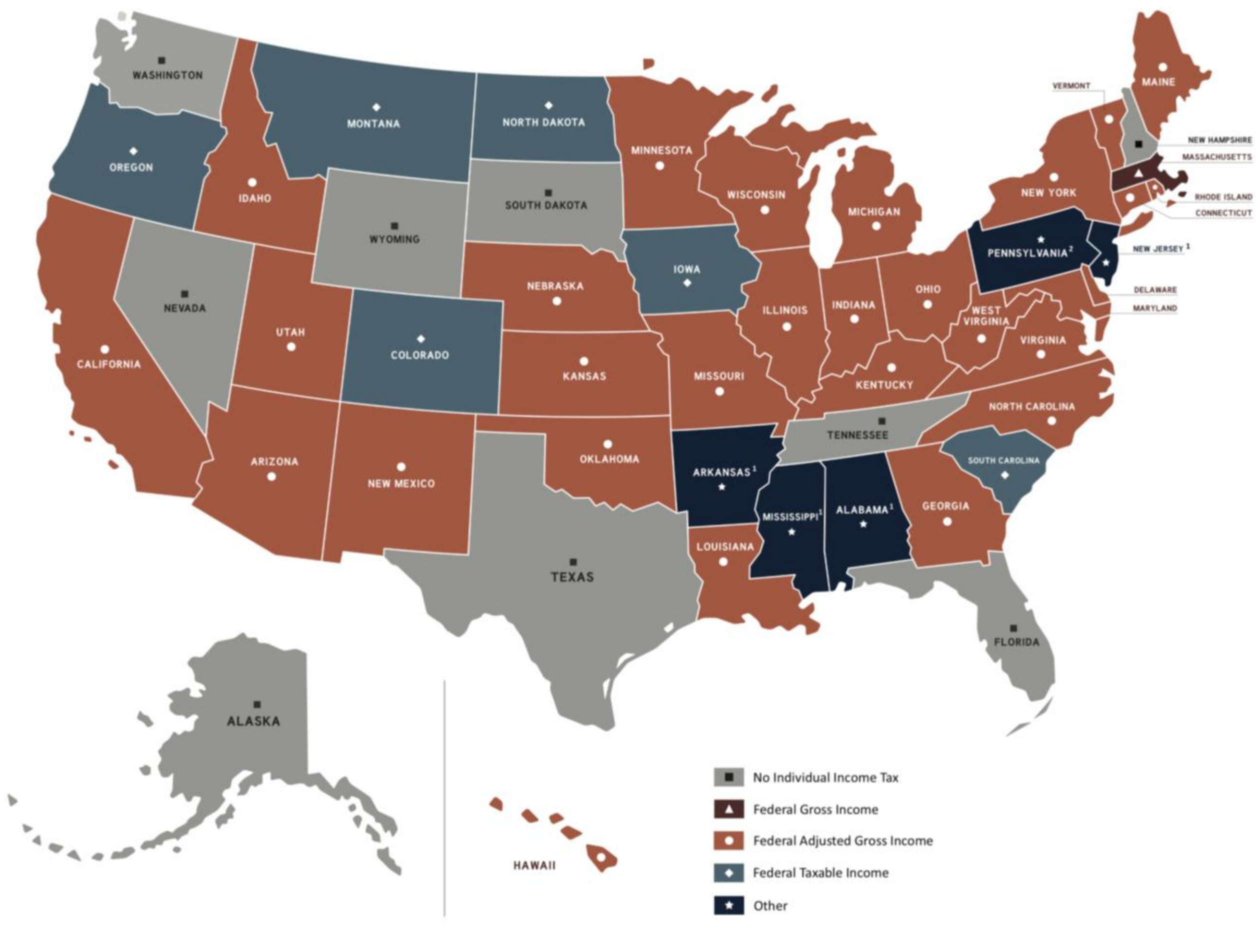
Colorado first began imposing an income tax in 1937. From 1937 to 1964, the State generally required taxpayers to calculate their state taxable income independently from federal tax law. In 1964, the General Assembly enacted the Colorado Income Tax Act of 1964 [House Bill 64-1003], which provided that Colorado taxable income would be calculated based on federal tax laws in tax years beginning after December 31, 1964. The General Assembly stated that its intent for using federal law as the basis for calculating Colorado taxable income was "to (1) simplify preparation of state income tax returns, (2) aid interpretation of the state income tax law through increased use of federal judicial and administrative determinations and precedents, and (3) improve enforcement of the state income tax laws through better use of information obtained from federal income tax audits." Starting with the 1965 tax year, individuals used federal adjusted gross income as the starting point for calculating Colorado taxable income, and corporations, estates, and trusts used federal taxable income as the starting point, after which the taxpayers would make adjustments to their federal adjusted gross or taxable income as required by state law, to arrive at Colorado taxable income. In 1987, the General Assembly enacted the Colorado Income Tax Act of 1987 [House Bill 87-1331], which transitioned individuals from using federal adjusted gross income as the starting point to using federal taxable income as the starting point.

Other States Comparison

Many states with an individual income tax use a version of federal income as the starting point for calculating their state taxable income, such as federal gross income, federal adjusted gross income, or federal taxable income. As of March 2026, there are five other states (excluding Colorado) that use federal taxable income as the starting point for calculating state taxable income for individuals. The majority of states (29) with an individual income tax use federal adjusted gross income as the starting point for calculating state taxable income for individuals. One state (Massachusetts) uses federal gross income and five states use other approaches that do not use a federal starting point for individual taxpayers. Exhibit 4 shows the starting points for determining state taxable income for states with an individual income tax.

Exhibit 4

State Starting Points for Calculating State Taxable Income for Individuals, 2026



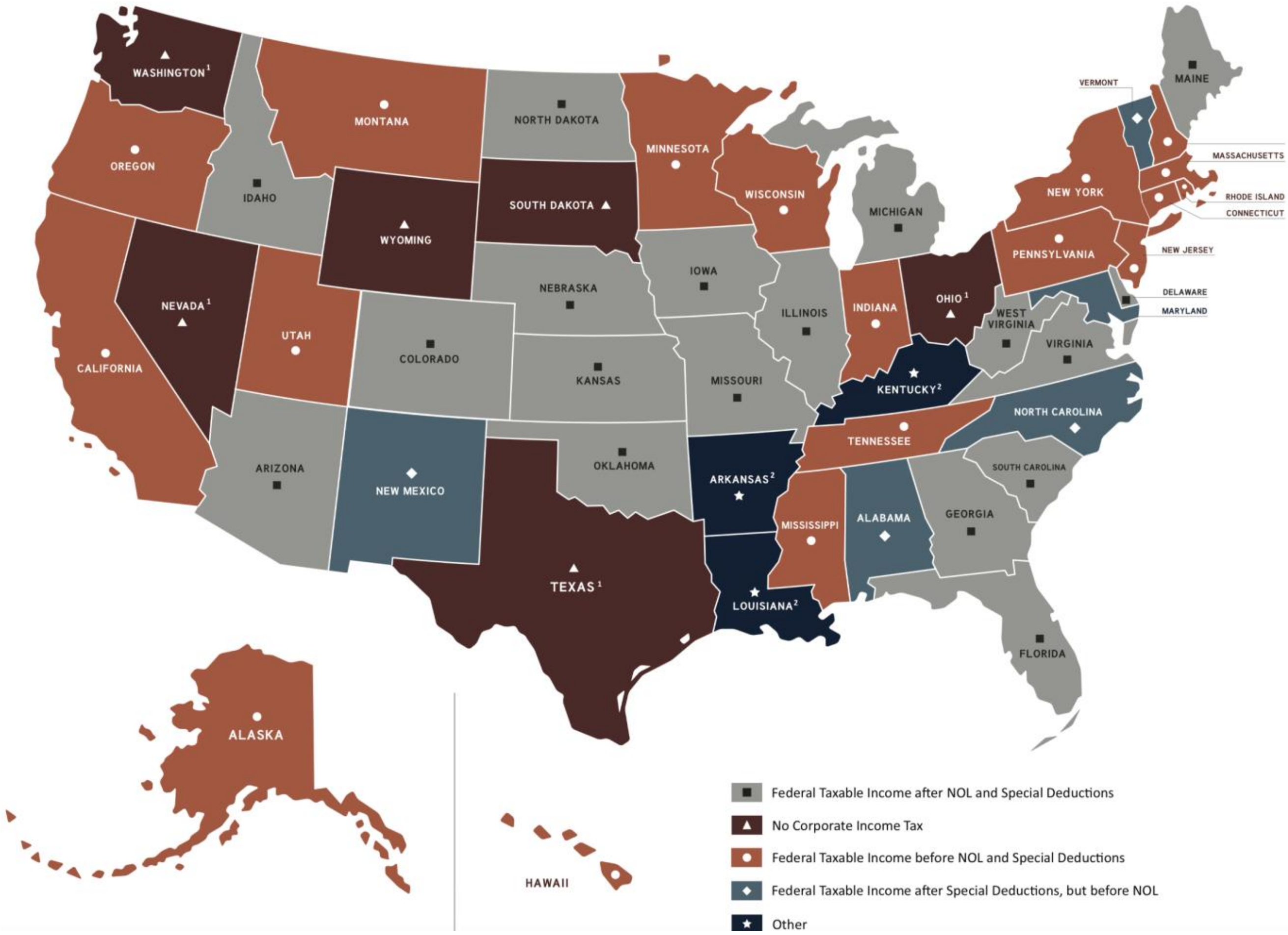
Source: Office of the State Auditor analysis of Bloomberg Law and other states' statutes.

[1] Alabama, Arkansas, Mississippi, and New Jersey do not use a federal starting point; instead, they use state gross income. In computing state taxable income, they incorporate some definitions from the IRC.

[2] Pennsylvania does not use a federal starting point; instead, Pennsylvania's state income tax is imposed at a flat rate on different types of income, such as compensation, gains, dividends, and interest.

Similar to individual income tax, many states with a corporate income tax use a version of federal income as the starting point for calculating state taxable income. However, for corporations, the starting points are typically different from individuals and include federal gross receipts; federal gross income; federal taxable income before the net operating loss (NOL) deduction and special deductions (such as the dividends received deduction); federal taxable income after the net operating loss deduction and special deductions; and federal taxable income after special deductions but before the net operating loss deduction. Net operating losses and special deductions for corporations are discussed later in the report. Colorado's starting point for calculating state taxable income for corporations is federal taxable income after the net operating loss deduction and special deductions; however, as discussed later in this report, Colorado has decoupled from the federal net operating loss provision in state law. As of March 2026, there are 17 other states (excluding Colorado) with a corporate income tax that also use federal taxable income after the net operating loss deduction and special deductions as the starting point for calculating state taxable income for corporations. There are 18 states with a corporate income tax that use federal taxable income before the net operating loss deduction and special deductions as the starting point and five states that use federal taxable income after special deductions but before the net operating loss deduction. Three states use other starting points. Specifically, one other state (Louisiana) uses federal gross receipts, another (Kentucky) uses federal gross income, and one (Arkansas) uses another starting point depending on whether the corporation operates only in Arkansas or in multiple states. Exhibit 5 shows the starting points for determining state taxable income for states with a corporate income tax.

Exhibit 5
State Starting Points for Calculating State Taxable Income for Corporations, 2026



Source: Office of the State Auditor analysis of Bloomberg Law and other states' statutes.

[1] Nevada, Ohio, Texas, and Washington do not impose corporate income taxes, but instead impose other taxes on businesses, including the Nevada Modified Business Tax, Ohio Commercial Activity Tax, Texas Franchise Tax, and Washington Business and Occupation Tax.

[2] In Arkansas, corporations that only operate in Arkansas use federal gross sales as the starting point for calculating state taxable income. For multistate corporations, the starting point is federal taxable income before net operating losses and special deductions. Louisiana uses federal gross receipts as its starting point. Kentucky uses federal gross income as its starting point.

Incorporation of the IRC into the State's tax code (referred to as "conformity") is also an important factor when considering Colorado's tax base. Conformity concerns whether states automatically incorporate amendments to federal law into their own income tax laws by reference to the IRC. According to The Tax Adviser, which is the magazine for the American Institute of Certified Professional Accountants (AICPA), "States generally conform to the [Internal Revenue] Code to simplify the calculation of taxpayers' income taxes and to make the administration of the state tax system simpler and more efficient. These efficiencies of conformity, however, often butt up against other state policy concerns such as state budgets and state-specific incentives that do not necessarily align with those of the federal government. Further, as Congress inevitably continues to amend the

[Internal Revenue] Code, the federal policy goals animating those amendments may change over time, causing states to adjust their conformity to the [Internal Revenue] Code or limit their adoption of future changes."

Colorado conforms to the current version of the IRC for both corporate and individual taxpayers. As discussed, this is referred to as "rolling conformity." The Colorado General Assembly must pass legislation if it wants to decouple from new amendments to the IRC, and it has done so for many provisions, which are discussed throughout this report. Rolling conformity is common among the 40 other states with broad-based income taxes, with 19 of the 40 states (48 percent) having rolling conformity for their individual income tax. Of the other 43 states that impose a corporate income tax, 23 of the 43 states(53 percent) have rolling conformity.

Many states instead conform to the IRC as of a certain date. This is typically referred to as "static conformity." Seventeen other states (43 percent) with a broad-based income tax have static conformity for their individual income tax, and 18 (42 percent) have static conformity for their corporate income tax. There are a few other states that either do not conform to the IRC or selectively conform to it. For example, Mississippi does not conform to the IRC generally, but the IRC is incorporated by reference throughout the Mississippi tax statutes. Exhibit 6 shows how states conform to the IRC.

Exhibit 6
State Conformity to the Internal Revenue Code

Conformity Type	States
Rolling Conformity	Alabama, Alaska[1], Colorado, Connecticut, Delaware, Illinois, Iowa, Kansas, Louisiana, Maryland[2], Massachusetts[3], Michigan, Missouri, Montana, Nebraska, New Mexico, New York, North Dakota, Oklahoma, Oregon[4], Pennsylvania[5], Rhode Island, Tennessee[6], Utah
Static Conformity	Arizona, California, Florida[7], Georgia, Hawaii, Idaho, Indiana, Kentucky[8], Maine, Minnesota, North Carolina, New Hampshire[9], Ohio[10], South Carolina, Virginia[11], Vermont, West Virginia, Wisconsin
Selective Conformity	Arkansas, Mississippi
No Conformity	New Jersey, Pennsylvania[5]

Source: Office of the State Auditor analysis of Bloomberg Law and other state statutes.
[1] Alaska has rolling conformity for its corporate income tax. It does not have an individual income tax.
[2] Maryland conforms to the IRC on a rolling basis; however, if the Maryland Comptroller determines that amendments to the IRC will impact state income tax revenue by at least $5 million, the amendments are not automatically adopted by Maryland.
[3] Massachusetts has rolling conformity for its corporate income tax but static conformity for its individual income tax to the IRC in effect on January 1, 2024.
[4] Oregon has "rolling reconnection" to the IRC, which is effectively rolling conformity. According to Oregon's Legislative Revenue Office, "Since 1997 Oregon has frequently maintained an automatic connection to changes in taxable income as defined by the IRC. This policy of a continuous connection is known as "rolling reconnect." Under a rolling reconnect policy, the revenue impacts resulting from changes in federal taxable income are estimated as needed and then incorporated into the Oregon current law revenue forecast. While the Legislature continues to review and monitor federal tax changes each year, specific legislation disconnecting Oregon from federal law is required to avoid inherently adopting federal changes to the Oregon tax base."
[5] Pennsylvania has rolling conformity for its corporate income tax and no conformity for its individual income tax. Its individual income tax is imposed at a flat rate on different types of income (e.g., compensation, gains, interest, dividends).
[6] Tennessee has rolling conformity for its corporate income tax. It does not have an individual income tax.
[7] Florida has static conformity for its corporate income tax but regularly considers whether to adopt a more recent version of the IRC. It does not have an individual income tax.
[8] Kentucky conforms to the IRC in effect on December 31, 2024. It does not automatically adopt amendments to the IRC after that date unless they extend provisions already in effect.
[9] New Hampshire has static conformity for its corporate income tax. It does not have an individual income tax.
[10] Ohio has rolling conformity for its individual income tax. It does not have a corporate income tax; it instead imposes a Commercial Activity Tax, which does not involve conformity to the IRC.
[11] During the 2026 legislative session, Virginia suspended rolling conformity and implemented a fixed conformity date of December 31, 2025. The state will continue to automatically conform to any federal tax law amendment that extends the expiration date of a federal tax provision to which Virginia conforms or has previously conformed.

Impact of Colorado using Federal Taxable Income as its Tax Base

The impact of Colorado's policy of using federal taxable income as its tax base includes several components. First, and most directly, this policy has an impact on Colorado's tax revenue. For example, according to Department of Revenue (Department) data, in Tax Year 2021, which was the most recent year of data available, there were 2,571,140 individual Colorado income tax returns filed in Colorado by full-year Colorado residents. These returns included a total of about $2.6 billion in deductions from gross income, which resulted in $264.6 billion in federal adjusted gross income and $214.2 billion in federal taxable income. Based on these figures, we estimate that Colorado taxpayers claimed about $53.0 billion in federal deductions (calculated by adding the $2.6 billion in above-the-line deductions and $50.4 billion in below-the-line deductions, which we estimated by subtracting federal taxable income from adjusted gross income). Colorado partially offset this amount claimed through federal deductions by requiring addbacks (i.e., state-level additions to federal taxable income) totaling $3.9 billion, resulting in about a $49.1 billion difference in taxable income due to federal deductions being incorporated into Colorado taxable income. Based on Colorado's 4.50 percent income tax rate in 2021, this reduction in taxable income could have resulted in a reduction to state tax revenue of roughly $2.2 billion. However, the true revenue impact to the State is unknown because it is dependent on the policy choices Colorado would make in the absence of using federal taxable income as its tax base. For example, of the $49.1 billion in federal deductions in the previous example, $36.9 billion (about 75 percent) is due to the federal standard deduction and many states that do not use federal taxable income as their tax base allow some form of a standard deduction. Additionally, if Colorado used a different method for establishing Colorado taxable income, taxpayers would likely make different choices in order to minimize their tax liability, which would also have an impact on the revenue the State collects.

Second, Colorado's decision to use federal taxable income as its tax base means that the economic impacts of federal tax policies for determining federal taxable income are amplified in Colorado since they are automatically incorporated into Colorado's tax policies and increase the economic incentives created by federal policies. For example, to the extent that the federal deduction for home mortgage interest expenses encourages home ownership and offsets the cost of housing, these impacts are amplified in Colorado since the State's policy effectively applies the same deduction for the purposes of determining Colorado taxable income, thereby increasing the total tax benefit available to qualifying taxpayers. Similarly, since the federal government uses deductions (e.g., the standard deduction) in addition to tax rates to adjust how much individuals must pay as a percentage of their income (to make the tax code more or less progressive), these decisions will flow through to Colorado's tax policies. For example, if the federal government reduced the standard deduction amount without other changes, this would cause lower income earners to pay a higher effective tax rate, making the tax system less progressive and this policy would automatically be applied in Colorado. Congress recently enacted P.L. 119-21, known as "The One Big Beautiful Bill Act" (OBBBA), which contained many significant changes to federal taxable income that will flow through to the State. These are discussed in more detail later in this report.

Third, Colorado's tax policy eases the administrative burden on taxpayers and the Department. Specifically, taxpayers can use their federal tax returns to complete their state tax returns instead of having to start over for Colorado tax purposes. Additionally, the Department is able to leverage federal oversight and enforcement instead of having to administer and enforce an entirely separate tax system. Further, although the State could likely achieve similar efficiencies by using a different tax base, such as federal adjusted gross income, that is already calculated for federal tax purposes, the process of changing this system would likely cause disruptions for taxpayers who would need to adjust to a new system and require the Department to make large-scale administrative changes that would likely be costly.

In the sections that follow, and in related appendices, we provide information on the major federal tax provisions and their potential impact on Colorado. Overall, because the IRC and its related body of law is large and highly complicated, we have limited our review to the more significant provisions in federal tax code.

Calculation of Federal Gross Income

Federal gross income is broadly defined as "all income from whatever source derived" [26 USC 61(a)]. Federal law provides a non-exhaustive list of items that are considered to be income, including, for example, compensation for services (including fees, commissions, and fringe benefits), income derived from business, gains from dealings in property (e.g., capital gains), interest, dividends, pension benefits, and some social security benefits. Additionally, in Commissioner of Internal Revenue v. Glenshaw Glass Co. (1955), the U.S. Supreme Court gave a liberal construction to federal statute to tax all income and gains except those specifically exempted in law, referring to the statutory language as a "catchall" provision. Some notable items of income that have been determined by case law to be considered part of gross income include punitive damages (except in the case of wrongful death claims) and income derived from illegal activities, such as the sale of illegal drugs. **A list of the types of income that are specifically stated in federal law to be included in gross income can be found in Appendix A.** Colorado generally conforms to the federal definition of gross income; however, when Colorado law has decoupled from federal tax treatment of certain types of income, we note that in Appendix A.

Federal law explicitly provides that some types of income are excluded from federal gross income. According to estimates from the U.S. Treasury Department, at the federal level, the exclusions with the highest revenue impacts to the U.S. government are the exclusion for employer contributions for medical insurance premiums and medical care [26 USC 106(a) and (d)], which had an estimated revenue impact of about $279.2 billion, and exclusion of gain from sale of principal residence [26 USC 121], which reduced federal revenues by about $79.2 billion in federal Fiscal Year 2025. Other income exclusions that many taxpayers may be aware of are gifts and inheritance [26 USC 102], interest on state and local bonds [26 USC 103], qualified scholarships [26 USC 117], and qualified tuition program distributions (often referred to as 529 plans) [26 USC 529(c)(1)]. Because Colorado generally conforms with federal exclusions from gross income, federal exclusions also reduce Colorado taxable income and state tax collections. Although we did not identify state-specific data on the revenue impact of these exclusions, given their impact on federal revenues, they likely also have a significant impact on state revenues. **A list of the types of income that are specifically excluded from gross income can be found in Appendix B.** When Colorado law has decoupled from federal exclusions, we note that in Appendix B.

Deductions from Federal Gross Income—"Above-the-Line" Deductions

After federal gross income is determined, individuals are allowed to take certain deductions to determine federal adjusted gross income (AGI). As discussed, these are often referred to as "above-the-line" deductions, with "the line" being federal AGI. Examples of above-the-line deductions include trade or business deductions, certain expenses of elementary and secondary school teachers, interest on education loans, and amounts contributed to health savings accounts. According to Department reports, Colorado taxpayers claimed about $2.6 billion in above-the-line deductions on their federal returns in Tax Year 2021. Based on the State's tax rate of 4.50 percent, we estimate that these deductions could have reduced state revenue by as much as $118 million, although some taxpayers likely did not earn enough income to incur tax liability regardless of the deductions, so the actual amount is likely somewhat less. **A list of the above-the-line deductions with descriptions and data on claims (when available) can be found in Appendix C.** By setting its tax base as federal taxable income, Colorado has generally incorporated these deductions into its tax base; however, when Colorado law has decoupled from federal above-the-line deductions, we note that in Appendix C.

Additionally, Colorado has several tax expenditures that are means-tested based on federal AGI, meaning if a taxpayer has over a certain amount of federal AGI, they are not eligible for the State tax expenditures. For example, the Colorado Qualified Care Worker Credit [Section 39-22-566, C.R.S.] is only available to eligible taxpayers with $75,000 or less in federal AGI ($100,000 or less if filing a joint return). To the extent that changes to federal law impact the calculation of Colorado taxpayers' federal AGI, it may impact their eligibility for these State tax expenditures, which can, in turn, impact Colorado income tax revenue.

Deductions from Adjusted Gross Income—"Below-the-Line" Deductions

From AGI, individual taxpayers can deduct either the standard deduction amount or itemize additional deductions. Deductions taken from AGI are sometimes referred to as "below-the-line" deductions. For Tax Year 2026, the standard deduction amount is $16,100 for single taxpayers and married individuals filing separate returns; $32,200 for married couples filing jointly; and $24,150 for individuals filing as heads of households. If an individual is at least 65 years of age or blind, they can claim an additional standard deduction amount; this amount is $1,650 for Tax Year 2026 per eligible person for taxpayers filing joint returns and $2,050 for single filers. The OBBBA also created an additional $6,000 deduction for seniors, based on AGI, available for Tax Years 2025 through 2028. According to Internal Revenue Service (IRS) Statistics of Income data, in Tax Year 2022, which was the most recent year of data available, about 5.3 million people in Colorado filed approximately 3 million federal tax returns using Colorado addresses. The standard deduction was claimed on about 2.6 million (87 percent) of those returns, with standard deductions totaling about $46.6 billion. The additional standard deduction was claimed on about 459,000 returns, totaling about $973.2 million. Exhibit 7 shows the number of returns that claimed the standard deduction, the total amount of standard deductions for various AGI groups, and our estimated reduction in state tax revenue associated with the standard deduction.

Exhibit 7
Number of Federal Returns Filed Using a Colorado Address that Claimed the Standard Deduction and Total Amount of Standard Deductions, by Adjusted Gross Income, Tax Year 2022

		Size of Adjusted Gross Income				
	Total	$1 to $25,000	$25,000 to $100,000	$100,000 to $200,000	$200,000 to $1,000,000	$1,000,000 or more
Number of Returns Claiming the Standard Deduction	2,582,250	681,840	1,308,400	429,640	157,680	4,690
Percent of Total Returns[1]	87%	23%	44%	14%	5%	<0.5%
Percent of Total Returns in AGI Group	N/A	98%	93%	79%	59%	29%
Total Dollar Amount of Standard Deductions	$46.60 billion	$9.64 billion	$22.77 billion	$10.12 billion	$3.95 billion	$116.75 million
Estimated State Revenue Impact[2]	$2.05 billion	$424.25 million	$1 billion	$445.43 million	$173.70 million	$5.14 million

Source: Office of the State Auditor analysis of the most recent Internal Revenue Service Statistics of Income data available as of June 2026.
[1] Based on a total of 2,972,380 federal returns filed with Colorado addresses.
[2] We estimated the state revenue impact of this provision by multiplying the total dollar amount of standard deductions by the State's 2022 income tax rate (4.4 percent). Beginning in Tax Year 2023, Colorado statute [Section 39-22-104(3)(p.5), C.R.S.] requires that taxpayers with $300,000 or more in federal adjusted gross income add back to their federal taxable income when calculating Colorado taxable income any amount of itemized deductions or the standard deduction claimed that is over $12,000 for single filers and $16,000 for joint filers. This estimate does not account for this state addback since the state addback did not go into effect until Tax Year 2023.

If taxpayers qualify for itemized deductions in excess of the standard deduction amount, they will typically claim itemized deductions rather than the standard deduction. Itemized deductions include medical and dental expenses (if they exceed 7.5 percent of AGI), state and local taxes (limited to $40,000 and adjusted annual for inflation for individuals from Tax Years 2025 through 2029 and $10,000 thereafter), home mortgage interest, investment interest, charitable contributions, casualty and theft losses, and wagering losses. **Appendix D provides a list with descriptions of the itemized deductions as well as data from the IRS on claims of itemized deductions on federal returns for taxpayers who used a Colorado address.** By using federal taxable income as its tax base, Colorado conforms with most of these deductions; however, when Colorado law has decoupled from federal itemized deductions, we note that in Appendix D.

According to IRS Statistics of Income data, in Tax Year 2022, which was the most recent year of available data, about 342,000 (12 percent) of the 3 million federal returns filed by taxpayers using a Colorado address claimed itemized deductions rather than the standard deduction. Exhibit 8 shows the number of federal returns filed using a Colorado address that claimed itemized deductions, the total amount of itemized deductions for various adjusted gross income groups, and our estimate of the impact of itemized deductions on state tax revenue.

Exhibit 8
Number of Federal Returns Filed Using a Colorado Address that Claimed Itemized Deductions and Total Amount of Itemized Deductions, by Adjusted Gross Income, Tax Year 2022

		Size of Adjusted Gross Income				
	Total	$1 to $25,000	$25,000 to $100,000	$100,000 to $200,000	$200,000 to $1,000,000	$1,000,000 or more
Number of Returns Claiming Itemized Deductions	342,050	11,070	97,530	113,840	108,250	11,360
Percent of Total Returns[1]	12%[2]	<0.5%	3%	4%	4%	<0.5%
Percent of Total Returns in AGI Group	N/A	2%	7%	21%	41%	71%
Total Dollar Amount of Itemized Deductions	$13.0 billion	$276.17 million	$2.41 billion	$3.41 billion	$4.52 billion	$2.39 billion
Estimated State Revenue Impact[3]	$571.86 million	$12.15 million	$105.87 million	$150.12 million	$198.70 million	$105.03 million

Source: Office of the State Auditor analysis of the most recent Internal Revenue Service Statistics of Income data available as of June 2026

[1] Based on a total of 2,972,380 federal returns filed with Colorado addresses.

[2] The percentages of total returns claiming the standard and itemized deductions do not equal 100 percent because there were about 48,000 returns that had under $1 in adjusted gross income and did not claim either the standard deduction or itemized deductions.

[3] We estimated the state revenue impact of this provision by multiplying the total dollar amount of itemized deductions by the State's 2022 income tax rate (4.4 percent). This estimate does not account for state income tax addbacks required for itemized deductions. The State requires several addbacks of itemized deductions claimed at the federal level, including state income taxes deducted at the federal level and a charitable contribution deduction for a conservation easement for which the taxpayer is also claiming the Colorado Conservation Easement Credit. In Tax Year 2020, which was the most recent year of data available, Department of Revenue data showed that state income taxes were added back to 290,279 Colorado returns for a total amount of about $981.3 million added back, which would generate an estimated $44.7 million in state revenue (when applying the amount added back by the State 2020 income tax rate of 4.55 percent). The Department did not have any data available on the amount added back due to conservation easements that were claimed as charitable contributions on Colorado taxpayers' federal returns. Additionally, beginning in Tax Year 2023, Colorado statute [Section 39-22-104(3)(p.5), C.R.S.] requires that taxpayers with $300,000 or more in federal adjusted gross income add back to their federal taxable income when calculating Colorado taxable income any amount of itemized deductions or the standard deduction claimed that is over $12,000 for single filers and $16,000 for joint filers. This estimate does not account for this state addback since the state addback did not go into effect until Tax Year 2023.

Although Colorado generally conforms with federal deductions, state statute limits the ability of taxpayers with higher income to claim below-the-line deductions for state tax purposes. Regardless of whether a taxpayer claims the federal standard deduction or itemized deductions, for Tax Years 2026 and later, Colorado statute [Section 39-22-104(3)(p.7), C.R.S.] requires that taxpayers with $300,000 or more in federal AGI add back to their federal taxable income when calculating Colorado taxable income any amount of itemized deductions or the standard deduction claimed that is over $1,000 for single filers and $2,000 for joint filers. House Bill 22-1414, which was referred to voters in the November 2022 election as Proposition FF and passed, provided that revenue generated from this addback is to be used to fund the Healthy School Meals for All (HSMA) Program, which "allows public School Food Authorities…participating in the National School

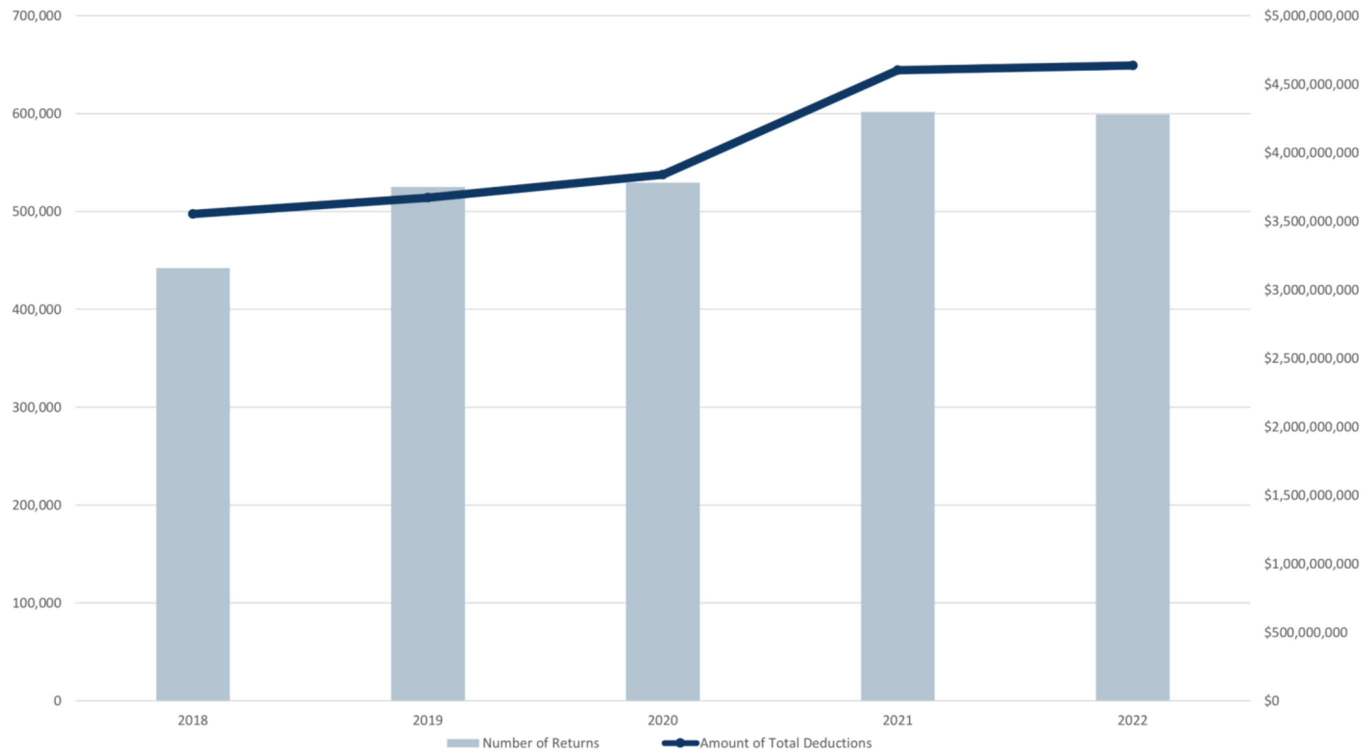
Lunch and School Breakfast Programs to provide free meals to all students." According to Legislative Council staff, preliminary data on collections for Tax Year 2025 indicate that about 146,000 tax returns with Proposition FF revenue totaling $114.2 million had been filed through June 1, 2026.

Qualified Business Income Deduction

After claiming either the standard deduction or itemized deductions, eligible taxpayers are also allowed to claim a deduction for qualified business income pursuant to 26 USC 199A. This deduction allows certain self-employed and small-business owners to claim a deduction for 20 percent of the qualified income from an eligible pass-through trade or business, such as a partnership. Certain types of businesses are subject to income-based limitations for this deduction, including health, law, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services, services consisting of investment and investment management, and trading of securities, partnership interests, or commodities. Colorado does not fully conform to this provision of the IRC. Specifically, there are two instances in which Colorado taxpayers must add back the amount of the Qualified Business Income Deduction claimed on their federal return when calculating Colorado taxable income. First, beginning in Tax Year 2018, if an individual is a partner or shareholder in a partnership or S corporation that makes a SALT Parity Act Election (to be taxed as an entity at the state level under Section 39-22-343, C.R.S.), the individual must add back the full amount of their Qualified Business Income Deduction [Section 39-22-104(3)(r), C.R.S.]. Second, beginning in Tax Year 2021, if a single filer has more than $500,000 in federal adjusted gross income or joint filers have over $1 million in federal adjusted gross income, they must add back the full amount of their Qualified Business Income Deduction. The addback is not required if the taxpayer files a Schedule F, which is generally required for farmers, with their federal returns [Section 39-22-104(3)(o), C.R.S.].

Exhibit 9 shows the number of federal returns filed using a Colorado address that claimed the Qualified Business Income Deduction and the total amount of Qualified Business Income Deductions from Tax Years 2018 to 2022, based on IRS data.

Exhibit 9
Number of Federal Returns Filed Using a Colorado Address that Claimed the Qualified Business Income Deduction and Total Amount of Qualified Business Income Deductions, Tax Years 2018 to 2022



Source: Office of the State Auditor analysis of the most recent Internal Revenue Service Statistics of Income data available as of June 2026.

Exhibit 10 shows the number of federal returns that were filed using a Colorado address that claimed the Qualified Business Income Deduction, the total amount of qualified business income deductions, and our estimate of the deductions' revenue impact to the State, for various AGI groups for Tax Year 2022, which was the most recent year of data available.

Exhibit 10
Number of Federal Returns Filed Using a Colorado Address that Claimed the Qualified Business Income Deduction and Total Amount of Qualified Business Income Deductions, by Adjusted Gross Income, Tax Year 2022

		Size of Adjusted Gross Income				
	Total	$1 to $25,000	$25,000 to $100,000	$100,000 to $500,000	$500,000 to $1,000,000	$1,000,000 or more
Total Returns	2,972,380	692,960	1,405,950	773,950	35,450	16,050
Number of Returns Claiming Qualified Business Income Deduction	599,030	39,020	238,220	287,150	22,740	11,900
Percent of Total Returns[1]	20%	1%	8%	10%	1%	<0.5%
Percent of Returns in AGI Group	N/A	6%	17%	37%	64%	74%
Total Dollar Amount of Qualified Business Income Deductions	$4.64 billion	$26.86 million	$579.62 million	$1.95 billion	$537.67 million	$1.54 billion
Estimated State Revenue Impact[2]	Up to $136.23 million	$1.18 million	$25.50 million	$85.90 million	Up to $23.66 million	Likely little to no revenue impact

Source: Office of the State Auditor analysis of the most recent Internal Revenue Service Statistics of Income data available as of June 2026.

[1] Percentages are based on a total of 2,972,380 federal returns filed with a Colorado address. Note that this table does not include about 48,000 returns that filed a return with under $1 of adjusted gross income. The Qualified Business Income Deduction was not claimed on any of those returns.

[2] To calculate the estimated state revenue impact, we multiplied the total dollar amount of Qualified Business Income Deductions in each AGI group by the 2022 Colorado income tax rate of 4.4 percent. These estimates have several limitations. First, for the total and all AGI groups, we were unable to determine which taxpayers had to add back their Qualified Business Income Deduction because of the pass-through entity from which they are getting the deduction made a SALT Parity Act election, which has the potential to decrease the state revenue impact in any of the AGI groups and the overall total. Second, we were unable to determine the revenue impact of the $500,000 to $1 million income group because we do not know the federal filing status of the claimants, and single filers with $500,000 in AGI are required to add back their Qualified Business Income Deduction but joint filers with over $500,000 but under $1 million in AGI are not. We estimated the maximum by multiplying the total dollar amount of Qualified Business Income Deductions in that AGI group by the Colorado 2022 income tax rate of 4.4 percent. Finally, deductions claimed by taxpayers with $1 million or more in AGI should generally not have a revenue impact on the State since taxpayers with over $1 million in AGI who claimed the deduction on their federal return are required to add it back when calculating Colorado taxable income; the exception to this is taxpayers in this AGI group who filed a federal Schedule F (for farming income), so federal deductions claimed by taxpayers in this AGI group who filed a Schedule F could have a revenue impact on the State.

Deduction for Charitable Contributions

Individual taxpayers who do not itemize their deductions but make charitable contributions are allowed to claim a deduction for the amount contributed, not in excess of $1000 (or $2000 for joint filers), if the contribution was made to a qualifying organization [26 USC 170(p)]. Department data shows that in Tax Year 2021, this deduction was claimed on 683,176 federal returns of taxpayers who also filed Colorado full-year resident returns for a total of $243.8 million in deductions.

Colorado conforms with the Federal Charitable Contribution Deduction for taxpayers who do not itemize deductions. We estimate that the revenue impact to the State associated with taxpayers claiming the federal deduction is about $11.0 million. Statute [Section 39-22-104(4)(m), C.R.S.] provides an additional state-level charitable contribution deduction for taxpayers who did not itemize their deductions on their federal returns that allows for a potentially larger deduction than at the federal level. The Colorado deduction is only allowed for the aggregate amount of charitable contributions over $500. According to Department data, in Tax Year 2022, the Colorado Charitable Contribution Deduction was claimed on 397,734 returns for a total revenue impact of about $40.9 million to the State.

Deduction for Qualified Tips

The OBBBA provided for a new, temporary deduction for certain tip income. For Tax Years 2025 through 2028, individual taxpayers (itemizers and non-itemizers) are able to deduct qualified tips received during a taxable year, not in excess of $25,000 [26 USC 63(b)(5), 224]. The deduction amount is reduced by $100 for each $1,000 by which the taxpayer's modified adjusted gross income exceeds $150,000 for single taxpayers and $300,000 for taxpayers filing jointly. The deduction is only available to employees who work in occupations that customarily and regularly received tips prior to 2025; the Secretary of the Treasury identifies these occupations. No deduction is allowed unless the taxpayer includes their social security number on their tax return. (See the recent and pending federal changes section for more detail on this provision.)

Deduction for Qualified Overtime Compensation

The OBBBA provided for a new deduction for certain overtime compensation. For Tax Years 2025 through 2028, individual taxpayers (both itemizers and non-itemizers) are able to deduct qualified overtime compensation, not to exceed $12,500 in a taxable year or $25,000 for joint filers [26 USC 63(b)(6), 225]. The amount of the deduction is reduced by $100 for each $1,000 by which the taxpayer's modified adjusted gross income exceeds $150,000 for single taxpayers or $300,000 for taxpayers filing jointly. Qualified overtime compensation means overtime compensation paid to an individual as required under Section 7 of the Fair Labor Standards Act (FLSA). Under this section of the FLSA, unless exempt, covered employees must receive overtime pay for hours worked greater than 40 in a workweek and at a rate not less than time and one-half their regular rates of pay. No deduction is allowed unless the taxpayer includes their social security number on their tax return. (See the recent and pending federal changes section for more detail on this provision.)

Colorado decoupled from this provision starting in Tax Year 2026, as part of House Bill 25-1296, which requires any overtime excluded or deducted from a taxpayer's federal gross income be added back for purposes of determining the taxpayer's state taxable income.

Deduction for Qualified Passenger Vehicle Loan Interest

The OBBBA provided a new, temporary deduction for certain auto loan interest. For Tax Years 2025 through 2028, individual taxpayers(both itemizers and nonitemizers) are able to deduct up to

$10,000 of qualified passenger vehicle loan interest [26 USC 63(b)(7), 163(h)(4)]. For higher-income taxpayers, the allowable deduction is reduced by $200 for each $1,000 by which the modified adjusted gross income of the taxpayer exceeds $100,000 in the taxable year for single filers and $200,000 for joint filers. Applicable passenger vehicles must have final assembly within the United States. (See the recent and pending federal changes section for more detail on this provision.)

Enhanced Senior Deduction

The OBBBA provided for an enhancement of the standard deduction for qualified senior citizens for Tax Years 2025 through 2028, which is in addition to the standard deduction for seniors available under existing law. The bonus amount is $6,000 and is available to taxpayers who have attained age 65 before the close of the taxable year. The amount is limited based on modified adjusted gross income; the $6,000 amount is reduced at a rate of 6 percent of modified AGI exceeding $75,000 in income for single filers and $150,000 for joint filers. It will also be available to qualifying persons who itemize their deduction in the amount allowed after considering the phase-out. Taxpayer's Social Security number must be included in the return to qualify [26 USC 151(d)(5)(C)]. (See the recent and pending federal changes section for more detail on this provision.)

Corporate Tax Deductions

According to Department data, in Tax Year 2023, there were 67,550 corporate returns filed in Colorado. These returns included a total of about $2.0 trillion in federal taxable income. After state adjustments were made, these returns collectively had about $16.7 billion in Colorado taxable income and corporations paid about $1.1 billion in Colorado income tax.

A significant amount of the federal deductions allowed for businesses fall under 26 USC 162, which broadly states, "There shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business…" This phrase has been the subject of judicial and regulatory interpretation. Whether an expense is "ordinary and necessary" often depends on the facts and circumstances of a particular business. "Carrying on" is also an important phrase, as it requires that business activities have actually begun in order to deduct expenses; therefore, expenses related to starting up a business are generally not deductible and must be capitalized and recovered over time.

26 USC 162(a) explicitly provides that deductions are allowed for the following: "(1) a reasonable allowance for salaries or other compensation for personal services actually rendered; (2) traveling expenses (including amounts expended for meals and lodging other than amounts which are lavish or extravagant under the circumstances) while away from home in the pursuit of a trade or business; and (3) rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity." Many other types of expenses not explicitly listed in 26 USC 162 are allowed to be claimed as ordinary and necessary business expenses under 26 USC 162; many of these have been established as deductible through regulatory action or case law. **A list of these other ordinary and necessary business expenses, with descriptions, is included in**

Appendix E. By using federal taxable income as its tax base, Colorado conforms with most of these deductions; however, when Colorado law has decoupled from federal business deductions, we note that in Appendix E.

Additionally, several other sections of the IRC provide deductions that can be claimed by businesses in a variety of industries, including, for example, amortization [26 USC 197], asset expensing [26 USC 179], charitable contributions [26 USC 170], and depreciation [26 USC 167 and 168]. **A list of these business deductions, which are available for many types of industries, is included in Appendix F.** By using federal taxable income as its tax base, Colorado conforms with most of these deductions; however, when Colorado law has decoupled from federal business deductions, we note that in Appendix F.

Federal law [26 USC 172] also allows corporations to claim a deduction for net operating losses. Colorado does not conform to the federal net operating loss deduction for corporations. Colorado statute [Section 39-22-304(2)(c), C.R.S.] requires that corporations add back their federal net operating loss deduction to federal taxable income when calculating Colorado taxable income. Statute then allows a deduction for the portion of the federal net operating loss that is allocated to Colorado. The Colorado Net Operating Loss Deduction is also limited to 80 percent of Colorado taxable income before the deduction is applied. Any Colorado net operating loss that is disallowed due to the 80 percent limitation, or that cannot be used due to insufficient taxable income, can be carried forward for up to 20 years. According to Department data, in Tax Year 2021, the federal net operating loss deduction was added back on 6,959 corporate returns for a total amount of about $159.5 billion added back. In that same year, the Colorado Net Operating Loss Deduction was claimed on 4,894 returns with a total of about $3.6 billion deducted, which resulted in a revenue impact of about $161.8 million to the State.

Corporations are allowed to claim additional “special deductions” when calculating federal taxable income, including dividends received deductions [26 USC 243, 245, and 245A], organizational expenditures [26 USC 248], and certain types of foreign source income [26 USC 250]. **These special deductions are described in Appendix G.** By using federal taxable income as its tax base, Colorado conforms with most of these deductions; however, when Colorado law has decoupled from federal special deductions, we note that in Appendix G.

The deductions discussed above apply to businesses across various industries. There are many types of businesses that operate in Colorado, such as farming, growing timber, producing oil and gas, extracting minerals, and print publishing, that have special tax rules and deductions that apply to them, such as the ability to deduct expenses that are specific to their type of business, such as film and television production costs (normally capitalized), circulation expenditures (normally capitalized), and depletion. Since these are typically industry-specific deductions, we did not include a comprehensive list or discussion of them in this report.

Tax Liability

After individual taxpayers have calculated their federal taxable income, they apply the marginal federal tax rates to it to determine their tax liability. In Tax Year 2026, the rates range from 10 percent to 37 percent. Lower amounts (referred to as "tax brackets") of income are taxed at a lower rate, with the rate increasing on higher amounts of income. Anything that happens "after" federal taxable income for federal tax purposes (i.e., applying federal tax rates or claiming federal credits) does not directly impact the calculation of Colorado taxable income since federal taxable income is the starting point. However, federal tax rates can impact Colorado's economy and total tax revenue by increasing or decreasing taxpayers' after-tax income.

After corporations have calculated their federal taxable income, they apply the federal tax rate to it to determine their tax liability. The federal corporate income tax is imposed at a flat rate of 21 percent. It is important to note that corporations that have income from business activities both within and outside of Colorado do not typically pay Colorado income tax on their entire federal taxable income. Rather, these corporations apportion and allocate their income among the jurisdictions in which they earn income.

Credits

After determining their tax liability, taxpayers subtract the value of any credits they are eligible to claim from their tax liability. Like the calculation of tax liability, federal credits do not directly impact the calculation of federal taxable income or taxable income for state tax purposes. However, changes to certain federal credits may impact Colorado income tax revenue since there are a few Colorado income tax credits that are calculated based on a percentage of a similar federal credit. These are the Child and Dependent Care Expenses Income Tax Credit [Section 39-22-119, C.R.S.], Colorado Earned Income Tax Credit [Section 39-22-123.5, C.R.S.], and Colorado Minimum Tax Credit [Section 39-22-105(3)(b), C.R.S.]. **Additional details about how these credits work, how they are calculated based on federal credits, the state revenue impacts of the credits, and links to our office's evaluations of the credits are provided in Appendix H.**

Federally Tax-Exempt Organizations

Colorado statute [Section 39-22-112(1), C.R.S.] provides that a "person or organization exempt from federal income taxation under the provisions of the internal revenue code shall also be exempt from the tax imposed by this article 22 [income tax] in each year in which such person or organization satisfies the requirements of the internal revenue code for exemption from federal income taxation…" Statute [Section 39-22-112(1), C.R.S.] further provides, "If the exemption applicable to any person or organization under the provisions of the internal revenue code is limited or qualified in any manner, the exemption from taxes imposed by this article 22 [income tax] shall be limited or qualified in a similar manner." Therefore, if organizations that operate in Colorado receive federal tax-exempt status, they also receive that status for Colorado income tax purposes and if they lose their federal tax-exempt status, they become subject to income taxes in Colorado.

Tax-exempt status under the IRC is largely determined under 26 USC 501. Common types of organizations that are exempt from federal income taxes include trusts created or organized in the United States that form a part of a stock bonus, pension, or profit-sharing plan of an employer for the exclusive benefit of its employees or their beneficiaries that is described in 26 USC 401(a); charitable, religious, educational, scientific, etc., organizations; business leagues; and certain political organizations. Most organizations that are exempt under 26 USC 501(c)(3) (charitable, religious, etc. organizations), 501(c)(4), and 501(c)(9) are required to apply to the IRS for recognition of their tax-exempt status. **A list of the types of organizations that are exempt from federal income tax is included in Appendix I.**

Recent and Pending Changes to Federal Law that Could Have an Impact on Colorado Taxable Income

Public Law 119-21

The OBBBA, Public Law 119-21, was the most significant piece of federal tax legislation since the 2017 Tax Cuts and Jobs Act (TCJA). The two acts are closely related. The TCJA made substantial changes to how federal taxable income is determined for both individual and corporate taxpayers, but many of the individual provisions were set to expire at the end of 2025. While the OBBBA incorporated several new tax provisions, the most significant from a federal revenue perspective involved extending expiring TCJA provisions, such as the enhancement of the increased standard deduction, the termination of personal exemptions, and the expansion of bonus depreciation.

While the TJCA increased revenue to the State due to broadening the definition of taxable income, the OBBBA is expected to decrease Colorado's personal and corporate income tax revenue, as base-broadening provisions were lessened compared to the TCJA and were outweighed by individual and business provisions that decreased taxable income, like expanded bonus depreciation, immediate research and development expensing, and an expanded deduction for Qualified Business Income. In total, Colorado Legislative Council staff expect the OBBBA to have the following revenue impact:

Exhibit 11

Colorado Legislative Council Staff OBBBA Fiscal Impact Estimate

	FY 2026	FY 2027	FY 2028
Individual	-$843.4 million	-$569.0 million	-$574.9 million
Corporate	-$336.3 million	-$151.3 million	-$149.7 million
Total Revenue Impact	**-1,179.7 million**	**-$720.3 million**	**-$724.5 million**

Source: Colorado Legislative Council staff, June 2025 Economic Forecast. Note: According to Legislative Council staff, the OBBBA's actual effect on state revenue will be more visible with complete spring filings season collections for March 2026 and April 2026. However, distinguishing OBBBA impacts from underlying economic changes will require more sophisticated tax data reports, which may not be available until the IRS shares its data extract with the Department of Revenue, which could occur in 2027 or 2028.

This section discusses new and expiring federal provisions in the order in which they are claimed/applied on federal income tax forms (e.g., above-the-line, below-the-line), then discusses other expiring/changing federal tax provisions separately. Although this list of provisions is not exhaustive, we have included provisions that we identified as potentially having more significant effects. When available, we have noted estimated federal and state revenue impacts. To assist our analysis of these provisions, we relied extensively on information materials provided by Bloomberg BNA, the IRS, the Multistate Tax Commission, and the federal Joint Committee on Taxation (JCT). It is important to note that the JCT, a nonpartisan committee of the U.S. Congress, provided two separate analyses projecting the fiscal impact of the OBBBA on the federal budget, one using a "current law baseline" and the other using a "current policy baseline". The current law baseline method calculates the difference in revenue by assuming that enacted laws will continue, temporary provisions will expire as scheduled, and discretionary spending will grow with inflation from current levels. Essentially, this method of calculation provided an estimate of the difference in revenue between a scenario where Congress passed the OBBBA, thereby continuing many of the provisions in the TCJA along with the new OBBBA provisions, and one where Congress took no action and allowed the temporary provisions in the TCJA to expire as scheduled. In contrast, the current policy baseline assumes that current laws continue and expiring provisions will be extended. This calculation method provided the difference in revenue between a scenario where the TCJA provisions would continue indefinitely and a scenario where Congress passed the OBBBA, essentially limiting the projected fiscal impact to the changes the OBBBA would make to the tax policies in place at the time the OBBBA was being considered. The current law baseline is the standard baseline for Congressional Budget Office projections, which the JCT typically uses for measuring the effects of proposed tax changes. However, Congress can request that the JCT provide a current policy baseline estimate instead, which it did for scoring the OBBBA. In some instances in this report, we cite estimates made using current policy baseline instead of the current law baseline because it more clearly illustrates the impact of the change in federal tax law on Colorado. For example, under the current law baseline, the elimination of personal exemptions, which originally occurred under the TCJA and was made permanent by the OBBBA, and creation of the enhanced senior deduction, which was a new provision in the OBBBA, were scored in tandem and estimated to be a revenue increase overall. Under the current policy baseline, there was no revenue gain from the elimination of personal exemptions, as they had already been suspended, so the estimate only reflects the revenue loss from the enhanced senior credit. This more accurately reflects the impact of the change on Colorado, which budgets on an annual basis and, therefore, will also not experience the elimination of the personal exemption as a revenue gain. Note that JCT estimates are specific to federal fiscal years, which begin on October 1 and end on September 30 of the next calendar year.

Other State Responses to the OBBBA

At least nine other states and Washington D.C. selectively decoupled from specific provisions (discussed in more detail in the following section) in 2025.

States including California, Delaware, Illinois, Maine, Maryland, Michigan, Pennsylvania, Rhode Island, Virginia, Washington D.C. have decoupled from various select provisions. Specifically:

- **Decoupled from IRC Section 168 Bonus Depreciation Provisions:** California, Delaware, Washington D.C., Illinois, Maine, Maryland, Michigan, Pennsylvania, and Virginia.

- **Decoupled from IRC Section 179 Increased Expensing Limits:** California, Michigan, and Virginia.

- **Decoupled from R&D Expensing:** California, Delaware, Washington D.C., Maryland, Maine, Michigan, Pennsylvania, Rhode Island, and Virginia.

- **Decoupled from Business Interest Deduction Limitation:** Maryland, Michigan, and Rhode Island.

- **Decoupled from New Deductions for Overtime and/or Tips:** Washington D.C. and Rhode Island

Additionally, although a minority of state legislatures had taken action to address the OBBBA or released guidance for their state taxpayers through 2025, surveys conducted by Bloomberg BNA suggest that many more anticipated legislation to do so in 2026 and expected more guidance to be released by state tax administrators.

The OBBBA Changes to Individual Income Tax Provisions

Moving Reimbursement Exclusion Extended

Description of Provision: Prior to the TCJA, qualified moving expense reimbursements from an employer to the employee/taxpayer were excludible from an employee's wage income, and therefore not subject to income or payroll tax; however, the TCJA suspended this exclusion for most taxpayers through 2025. The OBBBA made the temporary repeal of the household moving expense and reimbursement exclusion permanent. However, it also added an exception to this general rule for expenses and reimbursement of moves required of members of the U.S. intelligence community, along with members of the armed forces, meaning that these taxpayers can exclude employer-reimbursed moving expenses from income [26 USC 132(g)].

The JCT estimated that this provision, combined with the changes to the moving expense deduction noted below, would decrease federal revenues by $42 million in FY 2026 and by $86 million in FY 2027, relative to the current policy baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/2025.

Potential State Impact: Colorado conforms to the federal treatment of moving expense reimbursements under 26 USC 132(g). Relative to the exclusion that existed prior to the OBBBA, this provision will reduce state tax collections to the extent that members of the U.S. intelligence community who reside in the state take advantage of the benefit, but the impact will likely be small, based on the federal estimates.

Combat Zone Tax Benefits for Members of Armed Forces in the Sinai Peninsula Extended and Amended

Description of Provision: Typically, combat zones are designated by the President in an Executive Order. Under the TCJA, the Sinai Peninsula was statutorily presumed to be a combat zone through the end of 2025, which entitled members of the armed forces serving there to several tax benefits, including income and payroll tax exemptions and special estate tax rules [Pub. L. No. 115-97, § 11026]. This designation followed an escalation of violence in the area by ISIS-affiliated militant groups in 2015. The OBBBA permanently extended this designation and expanded it to include Egypt, Kenya, Mali, Burkina Faso, and Chad as qualified hazardous duty areas and combat zones, allowing combat pay income exclusions for members of the Armed Forces serving in these areas.

The JCT estimated that this provision will reduce federal revenues by less than $500,000 in future fiscal years, relative to the current policy baseline.

Effective Date of Change: Applies 1/1/2026.

Potential State Impact: This provision will decrease FTI to the extent that there are Colorado taxpayers who are armed forces members serving in the specified areas. While we are not able to ascertain the number who are Colorado taxpayers, it is likely that this expanded benefit will not have a significant revenue impact in Colorado, given the relatively low federal revenue impact estimate noted above.

Changes to Transportation Benefits: Bicycle Commuter Reimbursement Eliminated/Other Transportation Fringe Benefits Modified

Description of Provision: A fringe benefit is a form of pay in addition to stated pay for the performance of services. Some forms of additional compensation are specifically designated as "fringe benefits" by the IRC. Prior to the TCJA, up to $20 per month of qualified employer reimbursements for bicycle commuting expenses were excludible from wage income, and, therefore, not subject to income or payroll tax. Under the TCJA, employer reimbursements for bike commuting expense were considered wage income until the end of 2025, at which point they would then be eligible for exclusion. The OBBBA permanently eliminated the qualified bicycle reimbursement exclusion. The new law also modified the inflation adjustment for the limitation on qualified fringe benefits under 132(f), which are still excludible from income, to make it more generous. Eligible expenses include, but are not limited to, transit passes, qualified parking, and commuter highway vehicles [26 USC 132(f)].

The JCT estimated these provisions, taken together, would reduce revenues by $81 million in FY 2026 and $231 million in FY 2027, relative to the current policy baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/2025.

Potential State Impact: Colorado conforms to the federal treatment of fringe benefits under 26 USC 132. Because the State already conformed to the suspension of the bicycle commuting reimbursement exclusion, its permanent elimination will not affect state taxable income. The more generous inflation adjustment for fringe transportation benefits will reduce state taxable income, although the impact will likely be small.

Moving Expense Deduction Limited

Description of Provision: Prior to the TCJA, taxpayers could deduct employment-related moving expenses if:

- The moving costs were not reimbursed by an employer,
- The new work location was a certain distance from the taxpayer's former home, and
- The taxpayer worked a minimum number of weeks in the first 1 or 2 years after the move.

The TCJA suspended this deduction for most taxpayers, with an exception for members of the Armed Forces. The OBBBA made this temporary limitation of the moving expense deduction permanent. In addition, it added expenses for moves required by members of the US intelligence community as an exception to the general rule, allowing these taxpayers to take a deduction, along with members of the armed forces [26 USC 127(k)].

The JCT estimated that this provision, combined with the changes to the moving expense reimbursement exclusion noted above, would decrease federal revenues by $42 million in FY 2026 and by $86 million in FY 2027, relative to the current policy baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/2025.

Potential State Impact: Colorado conforms to the federal treatment of moving expenses under 26 USC 217. These provisions should reduce state tax collections to the extent that members of the US intelligence community who reside in the state take advantage of the benefit, but the impact will likely be small, based on the federal estimates.

New: Exclusion for Interest on Loans for Rural or Agricultural Real Property

Description of Provision: The OBBBA creates a new provision that allows banks and other lending entities to exclude 25 percent of interest income on qualified loans secured by rural or agricultural real estate. It also changes coordination with tax-exempt disallowance rules under IRC Section 265. Previously, interest on qualifying loans used to purchase tax-exempt obligations was not deductible. Under the OBBBA, 25 percent of the adjusted basis of a qualified rural or agricultural real estate loan is treated as adjusted basis in a tax-exempt obligation for the purposes of IRC Section 265. Therefore, the interest expense attributable to the remaining 75 percent of the loan may remain deductible. [26 USC 139L].

The JCT estimated that this provision would reduce federal revenues by $60 million in FY 2026 and by $99 million in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to loans made after 7/4/2025.

Potential State Impact: Colorado conforms to 26 USC 139. This provision will reduce federal taxable income, but based on the federal estimate, the revenue impact to the State is unlikely to be significant.

Standard Deduction Increase (Potential for Significant Impact)

Description of Provision: The standard deduction reduces taxable income and ensures that only households with income above certain thresholds will owe income tax. The TCJA almost doubled the standard deduction, from $13,000 to $24,000 for joint filers and from $6,500 to $12,000 for single filers in Tax Year 2018. The amounts were indexed to inflation. Under the TCJA, the higher standard deduction amounts were scheduled to expire at the end of 2025. The OBBBA permanently increased the standard deduction from $12,000 to $15,750 for individuals ($31,500 for joint filers) and from $18,000 to $23,625 for heads of households; the amounts are adjusted annually for inflation [26 USC 63(c)(7)].

The JCT estimated under the current law baseline (i.e., assuming the expiration of the TCJA) that this provision would reduce federal revenues by $92.1 billion in FY 2026 and by $144.7 billion in FY 2027. Under the current policy baseline (i.e., assuming the continuation of TCJA provisions), the revenue impact was much smaller, estimated to reduce revenues by $19.0 billion in FY 2026 and $19.3 billion in FY 2027.

Effective Date of Change: Applies to tax years beginning after 12/31/2024.

Potential State Impact: Colorado generally conforms to the federal definition of taxable income, including the federal standard deduction. Legislative Council staff expect that increased deductions from federal adjusted gross income will result in reduced state tax revenue. The Office of State Planning and Budgeting estimated that the extension and enhancement of the increased standard deduction would reduce state revenues by $310 million to $450 million in FY 2026 and by $525 million to $770 million in FY 2027. This estimate used a current law baseline that assumes the expiration of the standard deduction increases enacted under the TCJA; thus, a substantial portion of the revenue reduction reflects a continuation of existing policy rather than a year-over-year decrease in state revenue.

State and Local Tax (SALT) Deduction Cap Extended with Amendments

Description of Provision: Prior to the TCJA, taxpayers could claim deductions for all of their state and local property taxes and the larger of either income or sales taxes. The TCJA established a $10,000 cap on the itemized deduction for state and local income, sales, and property taxes for individual taxpayers (referred to as the "SALT cap"), and set it to expire at the end of 2025. The OBBBA increased the limit on the SALT deduction to $40,000 beginning in Tax Year 2025. The deduction amounts are phased down by 30 percent of the amount that the taxpayer's modified AGI (i.e. AGI increased by certain foreign exclusions) exceeds a threshold of $500,000. For Tax Years 2026 through 2029, the maximum deductible amounts and phasedown thresholds are set at a level of 101 percent of the prior year's level. During this period, the phasedown may not reduce the deduction permitted below $10,000. For tax years beginning in 2030 and after, the deduction limit for all individual filers reverts back to $10,000 [26 USC 164(b)].

The JCT estimated this provision would reduce federal revenues by $34.2 billion in FY 2026 and $28.9 billion in FY 2027, relative to the current policy baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/2024.

Potential State Impact: The increased SALT cap at the federal level will decrease FTI by allowing itemizers to deduct more state and local income, sales, and property taxes. Colorado requires taxpayers to add back any state and local income taxes, but not property or sales taxes, deducted at the federal level for the purpose of determining Colorado taxable income, which will partially offset the change in FTI. However, Colorado, provides a state-level deduction against local property taxes, which uses the federal cap. Since the federal SALT cap is increasing, for many Colorado taxpayers, this higher cap will reduce both federal and state income tax liability because, 1) they will be able to claim an increased SALT deduction at the federal level, reducing their FTI, 2) they will not have to add back the portion of the federal deductions claimed for property and sales taxes, reducing FTI and Colorado taxable income, and 3) the new increased federal cap will apply to the State's property tax deduction, allowing some taxpayers to claim a larger state-level deduction. Legislative Council staff estimated that this provision would reduce state revenue for FYs 2026 through 2030, with positive or neutral revenue impacts thereafter. More specifically, in the near-term, the Office of State Planning and Budgeting estimated this provision would reduce revenues by $25 to 45 million in FYs 2026 and 2027.

In response to the TCJA's cap on state and local tax deductions, Colorado created a new pass-through entity (PTE) tax, known as the SALT Parity Act. S corporations or partnerships may annually elect to be subject to tax at the entity level, rather than through its owners through the individual income tax code. Since the federal cap on state and local deductions only applies to the individual income tax and not entity-level taxes, taxpayers who elect to be taxed at the entity level can deduct the full amount of their state and local taxes. This "workaround" reduces taxpayers' federal tax liability but does not reduce state tax revenue. The expanded SALT cap may reduce the number of entities that file under the PTE tax [Section 39-22-343, C.R.S.].

Mortgage Interest Deduction Limited

Description of Provision: Prior to the TCJA, taxpayers could deduct interest paid on the first $1 million of mortgage debt for a primary and/or secondary residence plus the interest on up to the first $100,000 in home equity debt. The TCJA limited the deductibility to the interest paid on the first $750,000 of mortgage debt on primary residences for new loans made after December 15, 2017 and eliminated the deductibility of interest for home equity debt, through 2025. According to Bloomberg BNA, the OBBBA permanently disallows the deduction for interest on home equity debt and limits the deduction for interest paid on a mortgage used to acquire a residence to interest paid on the first $750,000 of mortgage debt for loans made after December 15, 2017. It also adds a provision treating certain mortgage insurance premiums on acquisition debt as qualified residence interest [26 USC 163(h)(3)(F)].

Relative to the current policy baseline, the JCT estimated this change would reduce federal revenues by $104 million in FY 2026 and by $256 million in FY 2027.

Effective Date of Change: Applies to tax years beginning after 12/31/2025.

Potential State Impact: Colorado conforms to the federal treatment of personal interest, including the limitation of the deductions for mortgage interest under 26 USC 163 (h)(3)(F). The extension of the deduction limitation will not change federal taxable income, as it is a continuation of existing policy. However, the expansion of the deduction to include mortgage insurance premiums could reduce state revenue.

New: 0.5% Floor on Deduction for Charitable Contributions and Extended Deduction Limit

Description of Provision: Prior to the TCJA, itemized deductions for cash contributions to public charities were generally limited to 50 percent of the taxpayer's AGI [26 USC 170(b)(1)(A)]. The TCJA increased the limit on itemized deductions for cash donations ("cash" includes payments made by check, electronic funds transfer, debit/credit card, among others) to public charities from 50 percent to 60 percent of a taxpayer's AGI. The OBBBA further limited the itemized charitable contribution deduction by imposing a floor equal to 0.5 percent of the taxpayer's AGI before taxpayers are allowed to deduct their charitable contributions. Additionally, it makes permanent the TCJA's increase of the deduction limit for cash charitable contributions to 60 percent, and retains the 50 percent limit for non-cash contributions [26 USC 170(b)(1)(G)].

The JCT estimated that this provision would increase federal revenues by $1.3 billion in FY 2026 and by $7.1 billion in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/2025.

Potential State Impact: Colorado conforms to the federal treatment of charitable contributions limits. The extension of the deduction limit should not affect state tax collections. The new floor on charitable contributions will increase FTI by reducing the tax benefits of charitable giving for higher-income taxpayers. In total, the Office of State Planning and Budgeting estimated that this provision would increase state revenues by $2 million to $7 million in FY 2026 and by $20 million to $25 million in FY 2027.

Note: Colorado statute [Section 39-22-104(3)(p.7) C.R.S.] requires taxpayers who have a federal AGI equal to or exceeding $300,000 to add back the amount of federal deductions (standard or itemized) that exceed $1,000 if filing a single return or $2,000 if married and filing jointly. To the extent that a taxpayer's charitable contributions exceed this limit, they would be required to add back deducted charitable contributions when calculating Colorado taxable income.

Personal Casualty Loss Deduction Limitation Extended

Description of Provision: Federal code provides a deduction for uninsured casualty and theft losses of more than $100 each, to the extent that total losses during the year exceed 10 percent of the taxpayer's adjusted gross income. The TCJA created a new limitation that taxpayers can only claim a deduction for uninsured personal casualty losses associated with a disaster declared by the President. The limitation was set to expire at the end of 2025. The OBBBA permanently extended the casualty loss deduction limitation but expanded the definition of qualifying disasters to include state-declared disasters [26 USC 165(h)(5)].

Relative to the current policy baseline, the JCT estimated that this expanded definition under OBBBA will reduce federal revenues by $27 million in FY 2026 and by $70 million in FY 2027.

Effective Date of Change: Applies to tax years beginning after 12/31/2025.

Potential State Impact: Colorado conforms to the federal deduction for losses. The extension of this provision should not affect FTI, but the expansion of the limitation to include state-declared disasters could potentially result in reduced revenues to the State in the event of a state-declared disaster resulting in casualty losses for Colorado taxpayers.

Special Rules for Disaster-Related Personal Casualty Losses Extended

Description of Provision: The OBBBA extended the special rules for qualified disaster-related personal-casualty losses under the Taxpayer Uncertainty and Disaster Relief Act of 2020. According to Bloomberg BNA, taxpayers affected by qualified disasters can deduct personal casualty losses above the line, without regard to whether aggregate net losses exceed 10 percent of a taxpayer's adjusted gross income and to the extent they exceed $500 per casualty [PL 116-260, Div. EE 304(b)]. Qualified disasters must have been declared during the period between 1/1/2020 and 9/2/2025 and must have had an incident period that began on or after 12/28/2019 and on or before 7/4/2025, ending no later than 8/3/2025.

The JCT estimated that this provision would reduce federal revenues by $52 million in FY 2026 with no fiscal impact in the following years, relative to the current policy baseline.

Effective Date of Change: 7/4/2025.

Potential State Impact: The extension of these rules should be revenue neutral for Colorado, as the State already conformed to the federal treatment of personal casualty losses.

Changes to Wagering Losses Deduction Extended and Amended

Description of Provision: Gambling winnings are often paid in cash. According to Bloomberg Law, in 1934, Congress created a limitation on the losses that a gambler may deduct in order to encourage reporting of this income. Taxpayers who itemize their deductions can deduct gambling losses, provided they do not exceed winnings included in gross income. In addition, federal tax courts had determined that professional gamblers could deduct non-wagering expenses (such as transportation to and from the casino) in excess of net gambling winnings. The TCJA disallowed the deduction of non-wagering expenses in excess of net gambling winnings and clarified that the limitation on losses applies to any deductible expenses incurred in carrying on the gambling activity. This provision was described by a House of Representatives Committee report as intended "to clarify that the limitation on losses from wagering transactions applies not only to the actual costs of wagers incurred by an individual, but to other expenses incurred by the individual in connection with the conduct of that individual's gambling activity."

The OBBBA extended this expiring provision and further limited the deduction to 90 percent of losses, to the extent of gains. As a result, 10 percent of otherwise deductible wagering losses are no longer deductible [26 USC 165(d)].

The JCT estimated that this provision will increase federal revenues by less than $500,000 in FY 2026 and by $120 million in FY 2027, relative to the current policy baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/2025.

Potential State Impact: Colorado conforms to the federal deduction for losses. This provision will increase federal taxable income and state revenue collections.

Miscellaneous Expenses Deduction Permanently Eliminated

Description of Provision: Prior to the TCJA, taxpayers who itemize deductions could deduct miscellaneous expenses to the extent that such expenses collectively exceed 2 percent of their AGI. Eligible expenses included unreimbursed employee expenses, tax preparation fees, credit and debit card convenience fees, fees to collect interest and dividends, and certain other expenses. The TCJA eliminated this deduction for the most part, although certain unreimbursed employee business expenses may still be deductible. The OBBBA permanently extends the suspension of miscellaneous itemized deductions from the previous sunset of 2025, but allows an itemized deduction for unreimbursed educator expenses [26 USC 67(g)].

The JCT estimated that this provision would decrease federal revenues by $9 million in FY 2026 and by $23 million in FY 2027, relative to the current policy baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/2025.

Potential State Impact: Colorado conforms to the federal treatment of miscellaneous itemized deductions. Because the State already conformed to the temporary suspension of these deductions, their permanent repeal should not affect state tax collections compared to prior years since the TCJA was enacted. However, because the expiration of the suspension on miscellaneous deduction would have allowed taxpayers to begin claiming additional deductions, the Office of State Planning and Budgeting estimated a revenue gain of $30 million to $35 million in FY 2026 and $70 million to $80 million in FY 2027, compared to what would have happened if the suspension had been allowed to expire.

The deduction for unreimbursed educator expenses, will reduce taxable income and state tax collections because it is a new provision under the OBBBA.

Repeal and Replacement of Pease Limitation

Description of Provision: For taxpayers with AGI above certain thresholds who itemized deductions, a mechanism known as the "Pease Limitation" reduced the total amount of itemized deductions by 3 percent of the amount by which the taxpayer's AGI exceeded the applicable threshold. The Pease Limitation was temporarily suspended by the TCJA and was set to be re-implemented in 2026. The OBBBA permanently repealed the Pease itemized deduction limitation and created a new limit with a new calculation. According to Bloomberg BNA, for taxpayers in the top income tax bracket (37 percent), the new limitation reduces itemized deductions by 2/37ths of the lesser of: (i) itemized deduction amount; or (ii) amount of taxable income exceeding the threshold found in §1(j) for taxpayers in the 37 percent tax bracket. The revised limitation does not apply to the §199A qualified business income deduction [26 USC 68].

The JCT estimated under a current policy baseline that this provision would increase federal revenues by $1.4 billion in FY 2026 and $3.5 billion in FY 2027.

Effective Date of Change: Expires 12/31/2025.

Potential State Impact: Colorado conformed to the federal provision imposing a limit on itemized deductions under IRC section 68 and will conform to this new limitation as well. According to Legislative Council staff, this provision is expected to slightly increase state income tax revenue, on net as it should increase taxable income.

Because Colorado already limits the amount taxpayers with higher incomes can deduct, the revenue impact to the State will likely be less significant than at the federal level. However, this change could impact Colorado's Healthy School Meals for All Program (HSMA). Specifically, non-corporate taxpayers with $300,000 or more in federal AGI are required to addback a portion of their federal standard deduction or itemized deductions when computing their Colorado taxable income. Revenue generated from this addback is used to fund the HMSA Program; preliminary data on collections for tax year indicate that 146,000 returns with revenue totaling $114.2 million had been filed through June 1, 2026, according to Legislative Council staff. To the extent that federal itemized deductions are reduced by the limit being reinstated, it may reduce the amount subject to the state HSMA addback and reduce the revenue generated for the program. However, Legislative Council staff projected that the OBBBA provisions that extend and expand increased standard deductions under the TCJA and modifications to other itemized deductions, like the increased cap on state and local tax deductions, would increase revenue to the HSMA program on net by $28.4 million in FY 2026 and $45.5 million in FY 2027.

Deduction for Pass-Through Business Income (199A Deduction) (Potential for Significant Impact)

Description of Provision: To equalize reductions in the corporate tax burdens for businesses that file through the individual income tax code (e.g., partnerships, S corporations), the TCJA created a deduction equal to 20 percent of qualified business income (QBI). QBI is the net amount of qualified items of income, gain, deduction, and loss from qualified trade or business [26 USC 199A]. The deduction is limited to the greater of 50 percent of the W-2 wages paid by the business, or 25 percent of W-2 wages plus 2.5 percent multiplied by the value of depreciable property. Certain types of businesses are subject to income-based limitations for this deduction, including health, law, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services, investment services or investment management services, and trading of securities, partnership interests, or commodities. This provision was scheduled to expire at the end of Tax Year 2025.

The OBBBA made the QBI deduction under the TCJA permanent, but it did not increase the rate. It also established a new minimum deduction of $400 (indexed for inflation) for taxpayers having at least $1,000 of QBI, along with other changes with regard to its computation.

The JCT estimated that this provision would reduce federal revenues by $388 million in FY 2026, and by $656 million in FY 2027, relative to the current policy baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/2025.

Potential State Impact: Colorado largely conforms with the federal deduction for QBI. However, a state-level modification is required for certain single filers with AGI over $500,000 and joint filers with AGI over $1 million, who must add back the full amount of their federal deduction. This addback does not apply if the taxpayer is required to file a schedule F (for farming and ranching) with their federal return. Additionally, if a partnership or S corporation elects to be taxed at the entity level for Colorado income tax purposes, all of its partners or shareholders must add back to their Colorado return all qualified business deductions claimed under 26 USC 199A on their federal return.

According to Legislative Council staff, this provision is expected to reduce state income tax revenue starting in FY 2026, but they were not able to estimate the amount. The Office of State Planning and Budgeting estimated it would reduce state tax collections by $130 million to $150 million in FY 2026 and by $220 million to $260 million in FY 2027.

Personal Exemptions Eliminated

Description of Provision: Personal exemptions were intended to reduce taxable income and ensure that only income above a basic level is subject to tax. They also link income tax liability to family size, reducing taxes for families with more dependents. Under the TCJA, the personal and dependent exemption amounts were reduced to zero with the revenue gain and impact on lower income taxpayers offset by the expanded standard deduction and expanded child tax credit. The personal exemption would have been $4,150 in 2018 for each taxpayer, spouse, and eligible dependent [26 USC 151 (d)(5)]. At the end of 2025, the personal exemptions were scheduled to revert to pre-TCJA levels and then be adjusted for inflation; however, the OBBBA permanently eliminated the personal exemptions.

The JCT estimated that this provision would increase federal revenues by $110.6 billion in FY 2026 and by $173.5 billion in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to taxable years beginning after 12/31/2024.

Potential State Impact: Colorado generally conforms to the federal definition of taxable income and conforms to the federal definition of dependent by reference to the personal exemptions for dependents. The Office of State Planning and Budgeting estimated that the termination of the personal exemption would increase revenues by $295 million to $430 million in FY 2026 and by $630 million to $925 million in FY 2027, relative to the personal exemption being restored if this provision had expired. However, because Colorado already conformed to the suspension of personal exemptions, their elimination will not affect state revenues.

New: Enhanced Deduction for Seniors (Potential for Significant Impact)

Description of Provision: The OBBBA created a new temporary deduction for seniors that is separate from the higher standard deduction. Seniors can claim this new deduction as well as the additional standard deduction for the aged or the blind. The deduction is available to individuals aged 65 or more at the close of the tax year, for Tax Years 2025 through 2028. The additional deduction amount is $6,000 per eligible individual and phases out at a rate of 6 percent of the taxpayer's modified AGI exceeding $75,000 in income for single and $150,000 for joint filers. It will also be available to qualifying persons who itemize their deductions in the amount allowed after considering the phase-out. Taxpayers must include their Social Security number on their return to qualify [26 USC 151(d)(5)(C)].

The JCT estimated that this provision would reduce federal revenues by $23.1 billion in FY 2026 and $23.0 billion in FY 2027, relative to the current policy baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/2024 and before 1/1/2029.

Potential State Impact: Since Colorado starts with federal taxable income for state tax purposes, the new bonus deduction for seniors will automatically apply to Colorado taxable income. According to Legislative Council staff, this provision is expected to reduce state income tax revenue from FY 2026 through FY 2029. The Tax Foundation estimated this provision would cost the State $126.6 in Tax Year 2026.

New: Auto Loan Interest Deduction

Description of Provision: The OBBBA established a new tax benefit, available for Tax Years 2025 through 2028, that allows a deduction for loan interest incurred to purchase an applicable passenger vehicle (excluding campers and RVs) with final assembly in the U.S. For qualifying vehicles, loan interest is deductible up to $10,000 per year, with the deduction phasing out by $200 for every $1,000 of modified AGI in excess of $100,000 for single filers or $200,000 for joint filers. A vehicle identification number is required to claim the deduction. The deduction is available to both itemizers and non-itemizers [26 USC 163(h)(4)].

The JCT estimated that this provision would reduce federal revenues by $5.4 billion in FY 2026 and by $8.1 billion in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to indebtedness incurred after 12/31/2024, for tax years beginning after 12/31/2024 and before 1/1/2029.

Potential State Impact: This provision reduces federal taxable income and flows through to Colorado taxable income; therefore, it will reduce Colorado taxable income and state revenue. The Office of State Planning and Budgeting estimated that this provision would reduce state revenues by $25 million to $40 million in FY 2026 and by $30 million to $40 million in FY 2027.

New: Charitable Contribution Deduction for Non-Itemizers Reinstated

Description of Provision: The OBBBA permanently reinstated the partial charitable contribution deduction for taxpayers who do not itemize their deductions and increased it to a maximum of $1,000 for single filers and $2,000 for joint filers. The deduction applies only to contributions made in cash and does not apply to a contribution to certain private foundations or any donor advised fund [26 USC 170(p)].

The JCT estimated that this provision would reduce federal revenues by $1.5 billion in FY 2026 and by $7.8 billion in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/2025.

Potential State Impact: Colorado conforms to the federal treatment of charitable contributions, including the new deduction provision. This provision will reduce FTI and, therefore, will reduce state tax collections. Note: The State currently has a state-level deduction that allows individuals who do not itemize deductions to subtract the amount of their charitable contribution in excess of $500. Therefore, conformity to the new federal provision will allow taxpayers to receive a double tax benefit for charitable donations over $500 but below the $1,000/$2,000 federal limit.

New: Deduction for Tip Income (Potential for Significant Impact)

Description of Provision: The OBBBA created an income tax deduction for qualified tips received by a taxpayer, available for Tax Years 2025 through 2028. The bill limited the amount of tip income that may be deducted to $25,000 per year regardless of filing status and phases out the deduction by $100 for each $1,000 of modified AGI exceeding $300,000 for married taxpayers filing jointly and $150,000 for all others. The bill defines "qualified tips" as cash tips received by an individual in an occupation that traditionally and customarily receives tips. The federal Secretary of the Treasury has published a list of "traditionally tipped occupations", which includes various occupations in the following industries: beverage and food service, hospitality and guest services, entertainment and events, home services, personal services, personal appearance and wellness, recreation and instruction, and transportation and delivery.

The deduction is limited to those amounts reported to the individual on Forms W-2, 1099-K, 1099-NEC, or reported by the taxpayer on form 4317. The bill contains a transition provision to allow those persons responsible for reporting tips to employees to approximate a separate accounting of that amount for Tax Year 2025. The deduction is available only if both the individual receiving the tip has a valid Social Security number. For federal purposes, the deduction for tips may be taken in addition to the standard deduction for taxpayers who do not itemize. The related FICA tip credit for businesses is also expanded to include Social Security taxes paid by an employer with respect to various beauty service businesses [26 USC 224, 63(b)(5)]. The Budget Lab at Yale estimates that there were roughly 4 million workers in tipped occupations in 2023, or about 2.5 percent of all employment. Among workers in the bottom half of hourly wages only 4 percent are in tipped professions.

The JCT estimated that this provision would reduce federal revenues by $10.1 billion in FY 2026 and by $7.7 billion in FY 2027, relative to the current law baseline.

Effective Date of Change: Both the deduction and expanded tip credit will be available for tax years beginning after 12/31/2024 and ending on or before 12/31/2028.

Potential State Impact: Colorado generally conforms to federal taxable income and has not decoupled from this provision; therefore, the reduction in federal taxable income from the deduction will also reduce Colorado taxable income. The Office of State Planning and Budgeting estimated that this provision would reduce state revenues by $45 million to $90 million in FY 2026 and by $50 million to $65 million in FY 2027.

New: Deduction for Overtime Pay
Description of Provision: The OBBBA created a new deduction for "qualified overtime compensation", defined as overtime compensation paid to an individual required under the Fair Labor Standards Act of 1938 that exceed the regular rate of pay at which the individual is employed. The deduction is available for Tax Years 2025 through 2028. Deductions are allowed only if the amount of overtime is reported separately on Form W-2; currently, overtime pay is included with regular pay in Box 1 on Form W-2. Any qualified tip income is ineligible for the deduction. Like the deduction for tips, the deduction will also be unavailable for any "highly compensated employee" or individuals lacking Social Security numbers and can be taken in addition to the standard deductions for taxpayers who do not itemize. The deduction for qualified overtime compensation is limited to $12,500 per year for single filers or $25,000 for joint filers. In addition, the bill phases out the deduction by $100 for each $1,000 of modified AGI exceeding $150,000 for single filers or $300,000 for joint filers [26 USC 225, 63(b)(6)]. The JCT estimated that this provision would reduce federal revenues by $32.8 billion in FY 2026 and by $25.7 billion in FY 2027, relative to the current law baseline.
Effective Date of Change: Available for tax years beginning after 12/31/2024 and ending on or before 1/1/2029.
Potential State Impact: Colorado decoupled from this provision preemptively, starting in Tax Year 2026, as part of House Bill 25-1296, which requires any overtime excluded or deducted from a taxpayer's federal gross income be added back for purposes of determining the taxpayer's state taxable income. However, due to the effective date of the law, the new federal deduction did impact the State in FY 2026. As a result, the Office of State Planning and Budgeting estimated that it would reduce revenues by $180 million to $290 million in FY 2026 and then cease to have an impact in the following fiscal years.

New: Tax-Exempt "Trump Accounts"

Description of Provision: Federal law provides for certain tax-advantaged savings accounts like individual retirement accounts (IRAs). The OBBBA provides for new, tax-exempt savings accounts, named "Trump accounts", for qualified children; Trump accounts are treated similarly to IRAs under IRC 408(a). Trump accounts are created on behalf of "eligible individuals," who must be under age 18 and have a valid Social Security number. Account contributions are permitted beginning July 4, 2026 and do not count against the regular IRA contribution limit.

Contributions to Trump accounts are limited to $5,000 annually, until the beneficiary turns 18, at which point nearly all of the special rules for Trump accounts cease to apply and are replaced by the section 408 rules that apply to other traditional IRAs. The contribution limit is indexed annually for inflation starting in Tax Year 2028, with exceptions for certain exempt contributions. Qualified contributions to a Trump account are excluded from the beneficiary's gross income. U.S. citizen children born after Dec. 31, 2024, but before Jan. 1, 2029, are eligible for a one-time initial government contribution of $1,000. Employers can also contribute up to $2,500 annually on behalf of their employees. Employer contributions do not count as gross income to the employee, but do count against the $5,000 limit noted above. Employer contributions to Trump accounts are deductible to the employer, but no deduction by an individual is allowed for any contribution to a Trump account.

Account distributions are generally not allowed before the first day of the calendar year in which the beneficiary turns 18, but this does not apply to rollovers from one Trump account to another, or rollovers from a Trump account to an ABLE account, if the beneficiary is age 17. As with traditional IRAs, any after-tax contributions made to the account are not taxable upon distribution [26 USC 530A,139J,6434,6659].

The JCT estimated that this provision would reduce federal revenues by $6.4 billion in FY 2026 and by $3.6 billion in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/2025.

Potential State Impact: Colorado conforms to the federal treatment of Trump accounts for income tax purposes. Given that employer contributions are excluded from employees' taxable income, this provision will reduce state revenues to the extent that employers would have provided other, taxable benefits to employees in the absence of the Trump accounts. State tax collections will be reduced further when the earliest Trump account beneficiaries turn 18 and become eligible to receive tax-free distributions, to the extent that the beneficiaries would have taken taxable distributions from other investment accounts in the absence of Trump accounts.

New: Treatment of Capital Gains from Sale of Certain Farmland Property

Description of Provision: The OBBBA created a new section in code that allows owners of qualified farmland who sell that land to a qualified farmer to elect to pay a portion of net income tax from the sale or exchange in four equal annual installments, rather than during the tax year of the transaction. Installments begin on the tax return due date for the taxable year in which the sale or exchange occurs, when the gain results from the sale or exchange, according to Bloomberg BNA [26 USC 1062].

The JCT estimated that this provision would reduce federal revenues by $765 million in FY 2026 and by $2.6 billion in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to sales or exchanges in tax years beginning after 7/4/2025.

Potential State Impact: This provision is a deferral of capital gain tax collections at the federal tax level, not a direct tax reduction. Rather than pay capital gains tax all at once, it allows taxpayers to spread payment across four annual installments. Due to the time value of money (i.e., a dollar collected today is worth more than a dollar collected four years from now), this should reduce federal tax collections. The State will not see the same revenue impact; Colorado generally conforms to federal treatment of capital gains, but has not adopted a similar installment payment mechanism.

Reinstated De Minimis Rules for Third Party Network Transactions

Description of Provision: Payment settlement entities (otherwise known as payment processing platforms) are required to report to the IRS and to businesses that receive payments through their platforms the gross amount of payments made in settlement of payment card transactions and third-party network transactions. However, there is an exception to this reporting requirement for de minimus payments, which changed under the OBBBA. Prior to the OBBBA, a payment processing company was required to report third party network transactions with any participating payee that exceeded a minimum threshold of $600 in aggregate payment, regardless of the number of transactions. Under OBBBA, reporting is no longer required by payment settlement entities if the aggregate number of transactions with a payee does not exceed 200 or if the aggregate amount does not exceed $20,000 [26 USC 6050W(e), 3406(b)].

Relative to the current law baseline, the JCT estimated that this provision would reduce federal revenues by $1.1 billion in FY 2026 and by $808 million in FY 2027 due to payees underreporting their income from third-party settlement organizations.

Effective Date of Change: Applies to calendar years beginning after 12/31/2024.

Potential State Impact: This provision will not have a direct impact on state taxable income, although reduced reporting requirements could lead to lower tax collections due to potential under reporting of income, which is reflected in the federal estimate.

Child Tax Credit (CTC) Increased and Expanded

Description of Provision: The maximum Child Tax Credit amount was temporarily increased to $2,000 under the TCJA, with lower income taxpayers eligible to receive up to $1,400 of the credit as a refundable credit (“the additional child tax credit”). Additionally, the TCJA increased the credit’s phase-out threshold to $200,000 for single filers and $400,000 for joint filers and an additional, nonrefundable $500 credit was established for any other dependent the taxpayer can claim (e.g., children over 16, dependents who are not eligible to be claimed under the Child Tax Credit, or full-time students). The OBBBA made permanent most of the TCJA provisions for the Child Tax Credit. Additionally, it increased the nonrefundable Child Tax Credit to $2,200 beginning in Tax Year 2025 and permanently indexed the nonrefundable credit to inflation beginning in Tax Year 2026. It also made permanent a requirement that the child’s Social Security number be included on the return and extends the Social Security number requirement to the taxpayer [26 USC 24(h)].

The JCT estimated that the OBBBA’s changes to the Child Tax Credit will decrease federal revenues by $10.4 billion in FY 2026, and by $6.6 billion in FY 2027, relative to the current policy baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/ 2024.

Potential State Impact: Colorado offers a refundable Child Tax Credit to individuals with at least one child under the age of six who claim, or could have claimed the federal credit. Colorado taxpayers claimed $89.2 million of state child tax credits in 2023. The amount of the state credit was a percentage of the federal credit through 2023. Starting on January 1, 2024, the state credit is a set amount that is based on the taxpayer's federal adjusted gross income. Therefore, a change to the federal credit should not directly affect the value of the state credit, although changes that affect taxpayer federal AGI calculations and other eligibility requirements, such as the requirement that a child’s Social Security number be included on the federal return, could have an indirect impact on the amounts claimed for Colorado’s Child Tax Credit to the extent that the changes limit taxpayers’ eligibility to claim a federal credit.

Child and Dependent Care Tax Credit Amended

Description of Provision: According to Bloomberg BNA, the OBBBA increases the amount of the Child and Dependent Care Credit from 35 percent to 50 percent of child and dependent care expenses, reduced (not below 35 percent) by 1 percent for each $2,000 by which AGI exceeds $15,000 and further reduced (not below 20 percent) by 1 percent for each $2,000 ($4,000 for joint filers) by which AGI exceeds $75,000 ($150,000 for joint filers) [26 USC 31(a)(2)].

The JCT estimated that this provision would reduce federal revenues by $409 million in FY 2026 and $1.2 billion in FY 2027, relative to the current policy baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/2025.

Potential State Impact: Colorado has a state-level Child and Dependent Care Credit that is tied to the federal credit. Colorado residents who claimed the federal credit for qualifying children on their federal tax return and have a federal adjusted gross income below $60,000 are allowed to claim the state credit. For Tax Years 2026 and later, the state credit is equal to 70 percent of the federal child and dependent care expenses credit the taxpayer claimed and was allowed for the same tax year (See Section 29-22-119, C.R.S.). Therefore, this provision, which increases the amount of the federal credit, will also increase the amount of state credits, thereby reducing state revenues.

New: Credit for Scholarship Granting Organizations (SGOs)
Description of Provision: The OBBBA established a new tax credit of up to $1,700 for cash contributions to organizations that grant scholarships for qualified elementary or secondary education expenses. It allows the credit to be carried forward up to 5 years. If a taxpayer claims the credit, they cannot also claim the charitable contribution deduction for the same contribution. Further, it creates an income exclusion for qualified elementary and secondary education scholarships from scholarship-granting organizations (SGOs). However, for contributions to an SGO to be eligible for this credit, the SGO must be listed on a state list of one or more covered states for the applicable calendar year. A covered state is defined as one of the states or the District of Columbia, that, for a calendar year, voluntarily elects to participate in the credit and identifies SGOs in the state [26 USC 25F and 139K]. The JCT estimated that this provision will reduce federal revenues by $501 million in FY 2027 and by $2.6 billion in FY 2028, relative to the current law baseline.
Effective Date of Change: Credit applies to tax years ending after 12/31/2026. Exclusions apply to tax years beginning after 12/31/2026.
Potential State Impact: Colorado has opted in to this new federal program. Taxpayers who would otherwise take the federal charitable contribution deduction for donations made to SGOs may take the credit instead (as noted, donations to SGOs are not eligible for both the charitable contribution deduction and the SGO credit). While the credit reduces taxpayers' overall tax liability, foregoing the charitable contribution deduction would increase taxpayers' FTI and state tax revenue.

Increased Exemption and Phaseout Amounts for Alternative Minimum Tax Extended with Amendments

Description of Provision: The individual Alternative Minimum Tax (AMT) was originally implemented in 1969 to ensure that high income earners who significantly benefit from certain federal tax provisions pay a minimum amount of tax relative to their income. Specifically, the federal AMT is calculated separately from, and paid in addition to, taxpayers' regular income tax to the extent that it exceeds their regular federal tax liability. To calculate the AMT, an individual first adds back various tax items, including personal exemptions and certain itemized deductions to regular income, which becomes the income base for the AMT. Taxpayers then subtract an AMT exemption amount and recalculate their tax using the AMT tax rate structure. AMT liability is the excess, if any, of this amount over the amount of tax owed under the regular income tax rules.

The TCJA retained the individual AMT, but temporarily raised the alternative minimum taxable income exemption amounts and increased the phase-out threshold, significantly reducing the number of taxpayers who owed AMT. The OBBBA permanently extended the increased AMT exemption amounts, increased the phaseout amount from 25 percent to 50 percent, and modified the inflation adjustment. In Tax Year 2026, the AMT is imposed at 26 percent of an individual's alternative minimum taxable income with an exemption amount of $90,100 for single filers and $140,200 for joint filers, with a higher rate of 28 percent applied to taxpayers with alternative minimum taxable incomes over $244,500. The threshold phaseout amounts are $500,000 for single filers and $1,000,000 for joint returns [26 USC 55].

The JCT estimated that this provision would increase federal revenues by $742 million in FY 2026 and by $1.3 billion in FY 2027, relative to the current policy baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/2025.

Potential State Impact: For individuals who are subject to the federal AMT, Colorado requires an addition to income for the amount by which AMT income exceeds regular FTI. Colorado AMT income is largely based on federal AMT income with the exception of an additional subtraction for any state and local bond interest. The state also conforms to the federal AMT exemption amount. According to the Department of Revenue, the changes to the AMT should not have a significant impact on the number of AMT taxpayers or state tax collections.

Achieving a Better Life Experience (ABLE) Account Changes

Description of Provision:

ABLE Account Contributions—ABLE accounts are tax-favored savings accounts to encourage qualifying disabled individuals to save money for certain disability-related expenses without losing eligibility for federal means-tested programs like Medicaid. Contributions to ABLE Accounts are not deductible for federal tax purposes, but funds distributed from ABLE accounts are excluded from FTI as long as all funds distributed from the account are used for qualified expenses. Generally, in a given year, an ABLE account cannot receive aggregate contributions in excess of the annual gift tax exclusion amount ($20,000 in 2026). The TCJA temporarily allowed individuals who are employed to contribute an additional amount, above the gift tax exclusion amount. The OBBBA made this expansion permanent [26 USC 529A(b)(2)(B)].

ABLE Account Saver's Credit—This provision, which allowed designated beneficiaries who make qualified contributions to their ABLE account to qualify for a nonrefundable credit of up to $1000, was set to expire at the end of 2025. The OBBBA permanently extended the credit and increased the credit amount to $2,100 [26 USC 25B(d)(1)].

529 to ABLE Account Rollover—Prior to the TCJA, all rollovers from 529 accounts, which are tax-favored accounts used for education expenses, to ABLE accounts were subject to taxation. The TCJA temporarily exempted from taxation rollovers from a 529 account to an ABLE account that were less than or equal to the annual ABLE contribution limit, provided that the accounts have the same designated beneficiary. The portion of the rollover in excess of the annual contribution limit was still taxable. The OBBBA made this allowance permanent [26 USC 529(c)(3)(C)(i)(III)].

The JCT estimated these provisions would each reduce federal revenues by less than $500,000 in future fiscal years, relative to the current policy baseline.

Effective Date of Change: Expires 12/31/2025.

Potential State Impact: Colorado conforms to federal rules related to ABLE accounts, except with regard to rollovers from 529 accounts, which are subject to recapture at the state level. Starting in Tax Year 2023, the State allows taxpayers to deduct the amount they contribute to ABLE accounts up to $20,000/$30,000 per beneficiary for single/joint filers, adjusted annually for inflation [Section 39-22-104(4)(i)(II)(B), C.R.S.]. The state deduction was schedule to expire at the end of Tax Year 2025, but was recently extended until January 1, 2031 by Senate Bill 25-302.

The extension of these federal ABLE provisions will not directly affect FTI and state tax collections will be unaffected but, to the extent taxpayers claimed the Saver's Credit or increased their state-deductible contributions to ABLE accounts due to the increased contribution limit, taxpayer liability will decrease.

529 Account Disbursements for Schooling Expenses and Postsecondary Credentialing Expenses

Description of Provision: 529 accounts are tax-favored accounts that taxpayers can use to save for education expenses. Distributions from 529 accounts are not subject to federal income tax as long as they are used for qualifying education expenses. The OBBBA expands the types of expenses that qualify to include a broad category of postsecondary credentialing expenses, including tuition, fees, books, supplies, and equipment required for the enrollment or attendance of a designated beneficiary in a recognized postsecondary credential program [26 USC 529(f)].

Further, the OBBBA expanded qualifying expenses to include certain expenses in connection with enrollment in or attendance at an elementary or secondary public, private, or religious school. For tax years beginning after Dec. 31, 2025, it also increased the annual aggregate per-beneficiary distribution limit from $10,000 to $20,000 [26 USC 529(c)(7)].

The JCT estimated that these provisions would reduce federal revenues by $22 million in FY 2026 and $39 million in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to distributions made after 7/4/2025.

Potential State Impact: According to the Department of Revenue, any distribution used to pay expenses for elementary or secondary school under IRC Section 529(c)(7) is a non-qualifying distribution for Colorado income tax purposes and must be added back to a taxpayer's Colorado taxable income. Therefore, the federal expansion of qualifying expenses for distributions used to pay for certain elementary and secondary school expenses would not apply for Colorado tax purposes.

Any distribution used to pay qualified higher education expenses under IRC Section 529(e)(3) is a qualifying distribution for Colorado income tax purposes [see Section 39-22-104(4)(i)(III)(A) and (4)(i)(IV)(B), C.R.S.]. Consequently, any distribution used to pay qualified postsecondary credentialing expenses under IRC Section 529(e)(3)(C) is a qualifying distribution for Colorado income tax purposes. Therefore, the expansion of postsecondary credentialling expenses at the federal level will reduce state revenues.

New: Direct Primary Care Service Arrangements

Description of Provision: A Health Savings Account (HSA) is a tax-advantaged account that individuals can use to save and pay for unreimbursed medical expenses (e.g., deductibles, co-payments, coinsurance, and services not covered by insurance.) The OBBBA expands HSA eligibility by allowing individuals enrolled in certain primary care-only, fixed-fee arrangements to contribute to an HSA. It also treats fees paid under these arrangements as qualified medical expenses excludible from income [26 USC 223]. The JCT estimated that this provision would reduce federal revenues by $94 million in FY 2026 and $177 million in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to months beginning after 12/31/2025.

Potential State Impact: Colorado conforms to this provision. Expanding the availability of HSAs could lead to more taxpayers reducing their gross income by making contributions to such accounts, which could lead to a reduction in state tax revenues.

New: Bronze and Catastrophic Plans for HSAs

Description of Provision: Prior to the OBBBA, individuals who purchased bronze plans and catastrophic plans available through an exchange under the Affordable Care Act, were generally not HSA eligible because they failed to satisfy the definition of a high-deductible health plan. The OBBBA treats these plans as high-deductible health plans compatible with Health Savings Account (HSA) requirements.

The JCT estimated that this provision would reduce federal revenues by $127 million in FY 2026 and $286 million in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to months beginning after 12/31/2025.

Potential State Impact: Colorado conforms to this provision. Expanding the availability of HSAs could lead to more taxpayers reducing their gross income by making contributions to such accounts, which could lead to a reduction in state revenues. According to the Devenir and HSA Council Demographic Survey, there were 1.02 million HSA accounts with an average balance of $4,190 in the state, as of the end of 2024.

The OBBBA Businesses Tax Provisions

Bonus Depreciation Reinstated (Potential for Significant Impact)
Description of Provision: The deduction for depreciation allows taxpayers to recover the cost of certain property over the life of the property, a practice known as capitalizing costs. It is an annual allowance for the wear and tear, deterioration, or obsolescence of the property and is deducted from the income of the business until the full cost of the property has been deducted. For example, a business that purchases equipment for $100,000 with a useful life of 10 years, might deduct $10,000 for depreciation on the equipment from its gross income for the next 10 years. Generally, due to the time value of money, it is advantageous for a business to deduct as much as is allowable for depreciation expenses each year, since this allows the business to reduce its tax liability in the short-term. Although claiming larger depreciation deductions earlier means that a business will not be able to claim as much in depreciation deductions in later years, the practice delays tax liability for the business and allows it to have more cash on hand that can be used for other purposes. Prior to the TCJA, a taxpayer generally had to capitalize the cost of property used in a trade or business or held for the production of income and recover such cost over several years through annual deductions for depreciation or amortization in accordance with a depreciation schedule applicable to the property. However, as a tax incentive, the Congress has historically passed provisions allowing for “bonus depreciation” which allowed taxpayers to claim depreciation expenses on an accelerated schedule. These provisions have typically been temporary and applied to only specific types of property. The TCJA temporarily allowed 100 percent bonus depreciation (i.e., full expensing) for Tax Years 2018 through 2022. In other words, firms were able to deduct the full value of capital expenses from taxable income in the year the expense occurred. After 2022, the bonus depreciation percentage was scheduled to decrease 20 percent each year until it was completely phased out at the end of 2026. Only qualified property was eligible for bonus depreciation, including property with a recovery period of 20 years or less, computer software, water utilities, and certain qualified film, television, theatrical, or sound productions [26 USC 168(k)]. The OBBBA made 100 percent bonus depreciation permanent, although taxpayers are not required to take the full deduction. The OBBBA also provides for special elections; taxpayers can elect a reduced, 40 percent deduction instead (60 percent for long production period property and qualified aircraft) for qualified property placed in service, and specified plants planted or grafted, during the first taxable year ending after January 19, 2025. The JCT estimated that this provision would reduce federal revenues by $65.1 billion in FY 2026 and by $65.2 billion in FY 2027, relative to the current law baseline.
Effective Date of Change: Applies to property acquired after 1/19/2025.
Potential State Impact: Colorado conforms to the federal treatment of bonus depreciation for individual and corporate filers. According to Legislative Council staff, the change to the bonus depreciation deduction is expected to reduce corporate and individual income tax revenue from businesses by significant but decreasing amounts beginning in FY 2026. The Office of State Planning and Budgeting estimated this provision would reduce state tax collections by $225 million to $315 million in FY 2026 and by $175 million to $250 million in FY 2027. These impacts are expected to decline over time, since by claiming larger deductions to reduce taxable income in the short-term, businesses will have less to deduct in future years, which will increase their taxable income.

Deduction for Research and Experimental Expenditures Reinstated (Potential for Significant Impact)

Description of Provision: Prior to the OBBBA, taxpayers were required to capitalize and amortize specified research or experimental expenditures deducted from income divided evenly over a 5-year period (or, in the case of expenditures attributable to research that is conducted outside of the United States, over a 15-year period.) The OBBBA provides for full expensing of domestic research and experimental expenditures with an election to amortize certain expenditures. It also allows small businesses to retroactively expense research and development expenditures incurred between 2022 and 2024, meaning these businesses could apply these costs as deductions against prior years' income, reducing their tax liability and potentially receiving refunds for a commensurate portion of prior years' taxes paid. Qualifying expenses include, among others: internal-use software development; patent fees and patent-related costs; abandoned, retired, or disposed of research and development projects; utilities; drawings and models; laboratory materials, and administrative and overhead costs [26 USC 174A, 174(d)].

The JCT estimated that this provision would reduce federal revenues by $33.6 billion in FY 2026 and by $20.5 billion in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to amounts paid or incurred in tax years beginning after 12/31/2024.

Potential State Impact: Colorado conforms to the federal deduction for research and experimental expenditures. Legislative Council staff reported that the amortization deduction is expected to reduce corporate and individual state income tax revenue from businesses by significant but decreasing amounts beginning in FY 2026. The Office of State Planning and Budgeting estimated this provision would reduce state tax collections by $225 million to $315 million in FY 2026 and by $40 million to $90 million in FY 2027.

New: Depreciation for Qualified Production Property (Potential for Significant Impact)

Description of Provision: According to Bloomberg BNA, the OBBBA provides an elective 100 percent bonus depreciation deduction (i.e., full expensing, allowing businesses to deduct the entire cost in the year it was incurred) for qualified production property placed in service before Jan. 1, 2031, with extension possible due to acts of God. Defines "qualified production property" to include any portion of nonresidential real property used as an integral part of qualified manufacturing, agricultural or chemical production, or refining of a "qualified product" (defined as "any tangible personal property, other than a food or beverage prepared in the same building as a retail establishment in which it is sold") that results in substantial transformation of the product [26 USC 168(n)].

The JCT estimated this provision would reduce federal revenues by $30.3 billion in FY 2026 and by $34.4 billion in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to property placed in service after 7/4/2025, but before 1/1/2031, construction of which begins after 1/19/2025, but before 1/1/2029.

Potential State Impact: Colorado conforms to the federal treatment of depreciation. Legislative Council staff expect the special depreciation allowance for qualified production properties to reduce state business income tax revenue over the next 6 years (FYs 2026 through 2031) before slightly increasing revenue. The Office of State Planning and Budgeting estimated that this provision would reduce state tax collections by $70 million to $95 million in FY 2026 and by $70 million to $130 million in FY 2027.

New: Qualified Sound Recording Productions

Description of Provision: Typically, taxpayers must capitalize the cost of property used in a trade or business or held to produce income and recover the cost over time through annual depreciation or amortization deductions. However, prior to the OBBBA, taxpayers could elect to treat the cost of any qualified film, television, or live theatrical production, subject to specified dollar limitations (typically $15 million, but $20 million in certain distressed areas), as an expense that is not chargeable to a capital account and, as a result, were fully deductible. These special expensing rules were available for any project that commenced before January 1, 2026. Additionally, 26 USC 168(k) allowed an additional first year depreciation deduction in the placed-in-service year of qualified property. "Qualified property" means property that has a recovery period of 20 years or less and includes computer software and water utility property. The TCJA increased the percentage of the additional first year depreciation deduction from 50 percent to 100 percent (i.e., 100 percent bonus depreciation) and expanded the property eligible for it to include certain film, television, or live theatrical productions. This provision was set to expire on December 31, 2026, but was made permanent as part of the OBBBA's extension of bonus depreciation noted earlier.

The OBBBA also expanded the elective expense deduction to include aggregate qualified sound recording production costs up to $150,000 per taxable year, to be included in the deduction of up to $15 million for production costs of qualified film, tv, or live theatrical productions produced and recorded in the U.S. Thus, only sound recordings that commence after the date of enactment and before January 1, 2026 are eligible for the deduction, which may be claimed in the taxable year that includes the commencement date. It also expands the definition of qualified property eligible for bonus depreciation to include qualified sound recording productions [26 USC 181(a)(2)(C), 181(f), 168(k)(2)].

The JCT estimated that this provision would reduce federal revenues by $369 million in FY 2026 and by $162 million in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to qualified sound recordings commencing in tax years ending after 7/4/2025.

Potential State Impact: Colorado conforms to the federal treatment of depreciation. The expanded special expensing rules and extended availability of bonus depreciation will reduce FTI and state tax collections.

Taxable Real Estate Investment Trust Subsidiary Asset Test Amended

Description of Provision: A real estate investment trust (REIT) is essentially a mutual fund corporation for real estate, providing a tax-favored vehicle through which an individual can invest in a professionally managed portfolio of real property. While REITs are generally able to avoid paying federal income taxes at the corporate level, there are many rules governing their initial qualification and they are limited in their ability to conduct an active business outside of real estate investment. A Taxable REIT Subsidiary (TRS) is a corporation that is owned directly or indirectly by a REIT and has jointly elected with the REIT to be treated as a TRS for tax purposes. A TRS can engage in all types of business activities and receive all types of income, including activities and income that would disqualify a REIT, and pays tax on any net income.

Prior to the OBBBA, the value of a REIT's total assets represented by one or more TRSs at the close of each quarter of the taxable year was limited to 20 percent. The OBBBA increased the limitation from 20 percent to 25 percent, increasing the value REITs can generate through supplementary business activity of its subsidiaries [26 USC 856(c)(4)(B)(ii)].

The JCT estimated that this provision would reduce federal revenues by $80 million in FY 2026 and by $185 million in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/2025.

Potential State Impact: Colorado generally conforms to the federal treatment of REITs; therefore, this provision should be expected to reduce state revenue as well.

Spaceports Under Exempt Facility Bond Rules

Description of Provision: State and local governments may issue tax-exempt facility bonds to finance airport infrastructure. Interest earned on these bonds is generally excluded from a taxpayer's gross income, but subject to applicable alternative minimum tax rules. The OBBBA expanded the definition of "exempt facilities" to treat spaceports like airports under the tax-exempt facility bond rules. The provision defines spaceport, adds special rules for the ground leases on land leased by a governmental entity, and exempts spaceports from federally guaranteed bond prohibition [26 USC 142].

The JCT estimated that this provision would reduce federal revenues by $11 million in FY 2026 and by $35 million in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to obligations issued after 7/4/2025.

Potential State Impact: To the extent that state and local bonds are issued for spaceport facilities, this provision will likely reduce state tax collections as investors in spaceport facility bonds will be able to exclude interest payments from FTI. However, such interest payments are classified as tax preference items that may be captured by the Alternative Minimum Tax.

1% Floor on Corporate Charitable Deduction

Description of Provision: Prior to the OBBBA, federal law allowed a charitable deduction for any charitable contribution payment made within the tax year, with total deductions for charitable contributions limited to 10 percent of the taxpayer's taxable income. The OBBBA limited the total charitable contribution deduction for corporations to a minimum of 1 percent and maximum of 10 percent of taxable income. Excess contributions can be carried forward up to 5 years on a first-in-first-out basis, reduced to the extent they reduce taxable income and increase net operating loss carryovers so as to eliminate a double tax benefit. The provision applies exceptions to certain farmers, ranchers and Native corporations [26 USC 170(b)(2), 170(d)(2)].

The JCT estimated that this provision would increase federal revenues by $1.3 billion in FY 2026 and by $1.9 billion in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/2025.

Potential State Impact: Colorado conforms to the federal treatment of corporate charitable contribution limits unless a taxpayer claims a Colorado credit for an item that is a federal charitable deduction, in which case, the donation amount related to the credit must be added back to FTI. This provision will increase FTI and state tax collections.

Asset Expensing Amended

Description of Provision: A taxpayer generally must capitalize the cost of property used in a trade or business and recover the cost over time through annual deductions for depreciation and amortization. Under Section 179 of the IRC, a taxpayer can elect to deduct the cost of qualifying property immediately upon being placed into service, rather than recover the cost through depreciation deductions. This deduction applies to tangible property, such as machinery and equipment purchased for business use, off-the-shelf computer software, and qualified real property. Prior to the OBBBA the maximum amount a taxpayer could expense was $1 million of the cost of qualifying property placed in service for the tax year. The $1 million amount was reduced by the amount by which the cost of qualifying property placed into service during the tax year exceeded $2.5 million. The OBBBA increased the maximum amount of Section 179 property that a taxpayer can expense to $2.5 million reduced by the amount by which the cost of qualifying property placed into service during the tax year exceeds $4 million. These limits are indexed for inflation for tax years beginning after 2025 [26 USC 179(b)].

Note: Some assets, such as machinery, equipment, office furniture, computers, and certain software could be eligible for both IRC 179 expensing and special bonus depreciation under IRC 168. If elected, Section 179 expensing would be applied first, and any amount expensed would reduce the remaining amount that could be deducted for the cost of the asset. Bonus depreciation could then be applied to the remaining deductible amount.

The JCT estimated that this provision would reduce federal revenues by $2.3 billion in FY 2025, $4.3 billion in FY 2026, and $3.6 billion in FY 2027.

Effective Date of Change: Applies to property placed in service in tax years beginning after 12/31/2024.

Potential State Impact: Colorado conforms to the federal asset expense election under IRC 179. The Office of State Planning and Budgeting estimated that this provision would reduce state revenues by $15 million to $25 million in FY 2026 and by $5 million to $15 million in FY 2027.

Percentage of Completion Method of Accounting Exception for Residential Construction Contracts

Description of Provision: The OBBBA expands favorable tax accounting rules for residential construction projects. Under prior law, residential construction contracts were required to use the "percentage of completion" method, which requires developers to recognize income based on costs incurred to date. However, there was a general exception from this requirement for certain "home construction contracts" (contracts for dwelling units in a building containing four or fewer units). The OBBBA allows these residential construction projects to use simplified accounting methods by broadening the general exception for home construction contracts to an exception for "residential construction contracts," which includes multifamily construction encompassing condominium and apartment projects. The OBBBA also increases the amount of time residential construction projects can take (from 2 years to 3 years) before certain tax cost capitalization rules under IRC 263A apply, giving projects more time to qualify for more favorable tax treatment during construction. It also repeals the existing special rule for residential contracts that are not home contracts. These changes enable developers of multifamily projects to delay income recognition, which may improve cash flow and reduce taxable income during long build cycles [26 USC 460(e)].

The JCT estimated that this provision would reduce federal revenues by $638 million in FY 2026 and by $557 million in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to contracts entered into in tax years beginning after 7/4/2025.

Potential State Impact: Colorado conforms to federal rules for computing taxable income for long-term contracts. This provision will reduce federal taxable income and state tax collections.

Payments from Partnerships to Partners for Property or Services

Description of Provision: Prior law stipulated that, under regulations to be issued by the Secretary of the Treasury, certain partnership transactions were to be treated as payment for property or services or a sale or exchange of property between a partnership and a non-partner, rather than as allocations and distributions from a partnership to a partner, which may be more favorable to the taxpayer. This provision was intended to close a loophole that taxpayers could use to disguise a sale of partnership interests as a more taxpayer-favorable transaction. However, the Treasury Department never finalized regulations for addressing disguised sales of partnership interests, leading some practitioners to argue that alternative treatment should be allowed for such transactions.

The OBBBA removed language requiring regulations to be issued. Thus, allocations and distributions that are in substance payments for property or services are treated as payments for property or services (disguised sales) rather than allocations and distributions from a partnership to a partner [26 USC 707(a)(2)].

The JCT estimated that this provision would increase federal revenues by $1.6 billion in FY 2026 and by $2.3 billion in FY 2027, relative to the current law baseline. This revenue increase reflected prevailing levels of noncompliance under prior law, not a change to tax liability.

Effective Date of Change: Applies to services performed and property transferred after 7/4/2025.

Potential State Impact: While this provision does not directly reduce FTI, it should deter taxpayers from continuing to capitalize on ambiguities in federal law and make it easier for the IRS to collect revenue as the result of an audit, which should also increase state tax collections.

Small Business Stock Gain Exclusion Expanded

Description of Provision: The OBBBA provides an exclusion from gross income of 50 percent of gain from the sale or exchange of qualified small business stock (QSBS) held for at least 5 years and acquired before Feb. 17, 2009, 75 percent when acquired between Feb. 17, 2009 and Sept. 27, 2010, and 100 percent when acquired after Sept. 27, 2010 and on or before July 4, 2025. For QSBS acquired after July 4, 2025, the exclusion is 50 percent when held for at least 3 years, 75 percent for at least 4 years, and 100 percent for at least 5 years, according to Bloomberg BNA.

The law also increased the maximum amount of gain that can be excluded from income for any single issuer of qualified small business stock to the greater of $15 million (from $10 million) or 10 times the aggregate adjusted basis in the stock. It also increases the aggregate gross assets threshold beyond which a business cannot be considered a qualified small business from $50 million to $75 million. Beginning in Tax Year 2027, the $15 million and $75 million limit are adjusted for inflation annually in the same manner as applies to the individual income tax rates and brackets under current federal law. According to a 2025 analysis by the Treasury Department, even prior to the expansion, the cost of the QSBS exclusion has "increased substantially over the past decade, peaking at over $40 billion for tax year 2021 before decreasing in 2022." It is primarily received by higher income taxpayers: "Taxpayers with average total positive income over $1 million account for 26 percent of returns claiming an exclusion and nearly 75 percent of gains excluded." [26 USC 1202].

Relative to the current law baseline, the JCT estimated that this provision would increase federal revenues by $56 million in FY 2026 and by $57 million in FY 2027 before causing a reduction in federal revenue (a $193 million revenue reduction in FY 2029, $1.2 billion in FY 2030, and $3.5 billion in FY 2031).

Effective Date of Change: See above

Potential State Impact: Colorado conforms to the federal treatment of small business stock and allows the full QSBS exclusion. The expanded QSBS exclusion will exclude more gains on the sale of stock from federal taxable income and, thus, reduce tax revenues. The Institute on Taxation and Economic Policy has estimated that the QSBS exemption would reduce Colorado revenues by $22.2 million in Tax Year 2026 and that the loss would grow over time.

Hydrogen Storage, Carbon Capture, Nuclear, and Geothermal Income for Publicly Traded Partnerships

Description of Provision: A partnership is generally treated as a pass-through entity for tax purposes, with income earned by the partnership not taxed at the business entity level, but taxed as income received by the partners as individual taxpayers. However, publicly traded partnerships are treated as corporations for federal tax purposes, meaning they must pay corporate income taxes on their income at the entity level and their owners must also pay taxes on income (dividends) they received from the partnership. An exception from this corporate tax treatment is provided for certain publicly traded partnerships if 90 percent or more of their gross income is "qualifying income."

The OBBBA adds to the definition of "qualifying income" income and gains derived from:

- transportation or storage of sustainable aviation fuel, liquified hydrogen, or compressed hydrogen;
- electricity generation, electricity storage, or carbon dioxide capture at a qualified carbon capture facility;
- electricity production from an advanced nuclear facility;
- electricity or thermal energy production using a geothermal or hydropower energy resource; and
- the operation of geothermal or ground water energy property.

Companies that generate 90 percent or more of gross income through these new sources will be eligible to be treated as pass-through entities not subject to corporate income tax. This allows these companies to avoid the taxation faced by C corporations, where earnings are taxed both at the corporate level and again at the shareholder level when distributed as dividends.

The JCT estimated that this provision would reduce federal revenues by $157 million in FY 2026 and by $325 million in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/2025.

Potential State Impact: Colorado generally conforms to the federal treatment of publicly traded partnerships. Accordingly, a publicly traded partnership that is treated as a corporation under IRC Section 7704 is generally treated as a corporation for Colorado income tax purposes. This provision will reduce state tax revenues.

Information Reporting Threshold for Certain Payees

Description of Provision: Prior to the OBBBA, persons engaged in a trade or business were required to report to the IRS payments to non-employees or vendors that required a 1099 form if the payments aggregated to $600 or more to a single payee in any tax year. The OBBBA increased this threshold to $2,000 and indexed it to adjust for inflation on an annual basis [26 USC 6041(a), 6041(h), 6041A(a)(2), 3406(b)(6)].

The JCT estimated that this provision would reduce federal revenues by $196 million in FY 2026 and $398 million in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/2025.

Potential State Impact: This provision will not have a direct impact on state taxable income. However, reduced reporting requirements could lead to lower state tax collections due to taxpayers potentially underreporting federal gross income.

Modified Adjusted Taxable Income Calculation for Business Interest Deduction

Description of Provision: Businesses can generally deduct the interest they pay or accrue on loans when calculating taxable income. However, federal law limits the amount of interest a business can deduct each year. In general, a business can deduct interest only up to the total of: 1) interest income, 2) 30 percent of adjusted taxable income, and 3) certain interest related to vehicle floor plan financing (i.e. costs incurred by auto dealerships for borrowing money to purchase vehicle inventory).

The OBBBA makes changes that generally allow businesses to deduct more interest expense. Beginning in tax years after Dec. 31, 2024, businesses can add back depreciation, amortization and depletion expenses when calculating adjusted taxable income for purposes of the interest limitation. Because this increases adjusted taxable income, it also increases the amount of interest businesses are allowed to deduct under IRC Section 163(j).

The OBBBA also changes the order in which the limitation applies beginning after Dec. 31, 2025; the limitation is first applied to capitalized interest and then to other interest expense [26 USC 163(j)(8)(A)(v), 163(j)(9)(C)].

The JCT estimated that this provision would reduce federal revenues by $8.3 billion in FY 2025, $6.5 billion in FY 2026, and $6.2 billion in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/2024.

Potential State Impact: Colorado conforms to this provision. According to Legislative Council staff, this provision is expected to increase interest deductions from federal taxable income, resulting in a loss of state income tax revenue beginning in FY 2026. The Office of State Planning and Budgeting estimated it would reduce state tax collections by $40 million to $50 million in FY 2026 and by $25 million to $30 million in FY 2027.

Definition of Adjusted Taxable Income for Business Interest Deduction

Description of Provision: In the calculation of Adjusted Taxable Income (ATI), the OBBBA disregards certain international tax items, such as certain foreign subsidiary income and related “gross-up” amounts and deductions connected to foreign-source income, with the effect of reducing the amount of the business interest deduction for some taxpayers. By reducing the amount of business interest that some businesses can deduct, this provision will increase federal taxable income.

The JCT estimated that this provision would increase federal revenues by $660 million in FY 2026 and by $1.4 billion in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/2025.

Potential State Impact: Colorado generally conforms to the federal treatment of business interest. This provision should increase state revenues.

New: Business Interest Limitation and Interest Capitalization

Description of Provision: Following the TCJA, which expanded limits on the deduction for business interest, and a period of rising interest rates, taxpayers turned to elective interest capitalization strategies, recharacterizing interest to other items that were not limited, like inventory. For example, a business that financed inventory purchases using borrowed funds could elect to capitalize the associated interest into the cost of the inventory, rather than deduct the interest amount as an expense. It could then recover the expense through costs of goods sold when it sells the inventory and avoid the business interest deduction limitation.

The OBBBA established a new provision that changes the requirements related to determining the business interest expense limitation and capitalizing interest. This new provision limits the benefit of elective interest capitalization [26 USC 163(j)(10)].

The JCT estimated that this provision would increase federal revenues by $360 million in FY 2026 and by $887 million in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/2025.

Potential State Impact: Colorado conforms to the federal treatment of personal interest, but requires an addition for the amount in excess of the limitation on net business interest under IRC 163(j), but there could be complexities depending on different methods of filing. Specifically, the federal limitation would generally be determined at the consolidated group level (i.e., a group of business entities connected through sufficient common ownership). However, many states, including Colorado, do not simply follow the consolidated group method of filing and require taxpayers to file separate entity returns or as a member of a state unitary combined group (i.e., a group of economically integrated business entities that are treated as a single economic enterprise). Therefore, the impact of these provisions on state tax collections is uncertain and could vary by filing method.

Limitation on Excess Business Losses of Noncorporate Taxpayers Extended

Description of Provision: Initially adopted by the TCJA and subsequently extended several times, a provision in the federal code disallows an “excess business loss” for a taxpayer other than a corporation. Essentially, the provision limits the extent to which taxpayers can use business losses to offset non-business income in the same tax year to no more than a threshold amount. An excess business loss in a tax year is the excess of aggregate deductions of a taxpayer attributable to trades or business of the taxpayer over the sum of the aggregate gross income or gain attributable to trades or business of the taxpayer plus a threshold amount, originally set at $250,000 and indexed for inflation (the threshold amount for Tax Year 2025 was $313,000). If aggregate business deductions create an excess business loss in a taxable year, it is treated as a net operating loss (NOL) and carried over into subsequent tax years under the applicable NOL carryover rules.

The limitation on excess businesses losses was set to expire on Jan. 1, 2029. The OBBBA permanently extends the disallowance of a deduction for excess business losses and retains treatment of the carryover amount as an NOL carryover. It also reset the inflation adjustment calculation for the limitation threshold, which had the effect of reducing the threshold amount from $313,000 in Tax Year 2025 to $256,000 in 2026 [26 USC 461(l)].

The JCT estimated that this provision would increase federal revenues by $107 million in FY 2026 and by $158 million in FY 2027, relative to the current law baseline.

Effective Date of Change: Loss disallowance applies to tax years beginning after 12/31/2026. Inflation adjustment applies to tax years beginning after 12/31/2025.

Potential State Impact: Colorado generally conforms to the federal definition of taxable income. There is no specific addback or subtraction for the excess business loss provision in IRC 461(l); therefore, changes to this provision under the OBBBA will increase FTI and state tax collections.

Business Meals Deduction Exception Amended

Description of Provision: Prior to the OBBBA, federal law allowed taxpayers to deduct the cost of certain business meals. In general, taxpayers could deduct 50 percent of the cost of business meals if the taxpayer (or an employee of the taxpayer) is present and the food or beverages are not considered lavish or extravagant. Deductions for certain internal food costs, such as employer convenience meals or employer-operated cafeterias, were set to expire at the end of 2025.

The OBBBA allowed the expiration of the deduction of certain internal food costs but provides an exception from the disallowance of expenses of employer-operated cafeterias for meals provided at the employer's convenience or expenses for goods or services (including use of facilities) sold by the taxpayer in a bonafide transaction for adequate and full consideration. Additionally, it excludes meals provided on certain fishing boats and at certain fish processing facilities from the 50 percent deduction limit and allows them to deduct the full amount [26 USC 274(o)].

The JCT estimated that this provision would reduce federal revenues by $42 million in FY 2026 and by $96 million in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to amounts paid or incurred after 12/31/2025.

Potential State Impact: For Tax Years 2024 through 2030, Colorado statute [Sections 39-22-104(3)(s)(I) and 304(2)(k)(I), C.R.S.] requires that taxpayers who claimed a deduction on their federal tax return for business meals add those back when calculating Colorado taxable income. Therefore, the changes under OBBBA, including the expansion of the deduction for commercial fishing vessels, should not impact state revenue.

Exclusion for Employer-provided Student Loan Payments Made Permanent

Description of Provision: Under section 127 of the IRC, an employee may exclude from gross income for income tax purposes, and employers may exclude from wages for employment taxes, up to $5,250 annually of educational assistance. “Educational assistance” means a payment, by an employer, of expenses incurred by or on behalf of the employee for their education including, but not limited to, tuition, fees, books, supplies, and equipment.

In 2020, the federal government temporarily expanded the definition of “educational assistance” to also exclude an employers’ payment of employees’ student loans from gross income. This exclusion for student loan payments was set to expire at the end of 2025. The OBBBA made this provision permanent and, starting in 2027, provides for an annual inflation adjustment for the $5,250 annual limit. As the Brookings Institute has pointed out, larger employers are more likely to provide a student loan repayment benefit, as such programs require some level of sophistication and investment. They are also more common among well-educated, white-collar professions; occupations with the highest access to student loan repayment programs include: nursing, health care, business, office-work, higher education, teaching, and sales [26 USC 127(c)(1)(B), 127(d)].

The JCT estimated that this provision would reduce federal revenues by $706 million in FY 2026 and $1.0 billion in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to payments made after 12/31/2025.

Potential State Impact: Colorado conforms to the federal exclusion of employer-provided educational assistance from an employee’s income. Because the State already conformed to this provision, its extension of this provision will not immediately decrease state tax collections. However, the new inflation adjustment will reduce state tax collections beginning in Tax Year 2027.

Energy Efficient Commercial Buildings Deduction Eliminated

Description of Provision: Prior to the OBBBA, building owners who placed in service energy efficient commercial building property or energy efficient commercial building retrofit property were able to claim a tax deduction. For property placed in service in 2023 and after, the deduction equaled the lesser of the cost of the installed property or the maximum energy savings per square foot. The OBBBA eliminated this provision for property beginning construction after June 30, 2026 [26 USC 179D(i)]. The JCT estimated no impact on federal revenue from this provision in FY 2026 and an increase of $6 million in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to property beginning construction after 6/30/2026.

Potential State Impact: Colorado generally conforms to IRC section 179 regarding the deduction for energy efficient commercial buildings. The elimination of this provision should increase state tax collections, although the revenue impact will likely be small, based on federal estimates.

Qualified Opportunity Zones

Description of Provision: The TCJA established the Opportunity Zone (OZ) tax incentives to spur private investment and economic activity in Qualified Opportunity Funds (QOFs) in designated low-income communities. A QOF is an investment vehicle organized as a corporation or partnership for the purposes of holding at least 90 percent of its assets in qualified opportunity zone (QOZ) property. Taxpayers who meet certain requirements may defer tax payments on qualifying capital gains by investing the capital gain into a QOF.

OZ investments under the TCJA provided several tax benefits to taxpayers, including (1) a temporary deferral of capital gains taxation if gains are reinvested in a QOF; (2) an increase in the investment basis (i.e., the initial amount of capital that is considered for tax purposes to have been invested, which could be used to offset capital gains and reduce tax liability when the investment is sold) if specific holding periods (5 or 7 years) were met; and (3) a permanent exclusion of the capital gains from income if investments in a QOF were held for at least 10 years (hence, these capital gains were not subject to taxation). After 2021, new investments no longer qualified for the 5-year and 7-year basis increases, but they were still eligible for the 10-year permanent exclusion. Investments held in QOFs had a mandatory gain recognition date of 12/31/2026.

The OBBBA permanently extended the OZ program beyond the 2026 gain-recognition date, and created new OZ investment opportunities for capital gains invested after that date. Under the new rules, deferred capital gains invested in a QOF receive a 10 percent basis increase after a five-year holding period. For investments in Qualified Rural Opportunity Funds, however, the basis increase grows to 30 percent of the deferred gain after five years. The additional basis increase previously available for investments held for seven years is eliminated. If a QOF investment is held for 10 years, taxpayers can increase the basis of the investment to its fair market value on date investment is sold or exchanged, which eliminates capital gains tax on all post-investment appreciation.

Additionally, the OBBBA narrows the definition of a “low-income” community, meaning that fewer census tracts will be eligible for designation as an OZ. The number of population census tracts in each state that can be designated as QOZs is generally not allowed to exceed 25 percent of the total number of low-income communities in the state. The OBBBA modified the substantial improvement threshold for improvements to property located in a QOZ that is comprised entirely of a rural area. As of July 4, 2025, the substantial improvement threshold for required additions to the basis for property located in these QOZs was reduced from 100 percent to 50 percent [26 USC 1400Z-1 and 1400Z-2].

The JCT estimated that this provision would initially increase federal revenues by $5.0 billion in FY 2026 and by $28.5 billion in FY 2027, and then reduce revenues by $5.4 billion in FY 2027 and by $4.7 billion in FY 2028, relative to the current policy baseline.

Effective Date of Change: Amendments to Opportunity Zone designations apply to areas designated after 7/4/2025. New rules pertaining to the deferral of capital gains invested in QOFs apply to amounts invested in QOFs after 12/31/2026. Amendments to the treatment of QOZ property apply to property acquired after 12/31/2026. The special rule for improvement of existing structures in rural areas applies 7/4/2025. Reporting requirements and penalties apply to tax years beginning after 7/4/2025.

Potential State Impact: Colorado conforms to the federal treatment of capital gains. Federal adoption of this provision will reduce individual state income tax collections initially, but could eventually lead to a revenue increase in future tax years as a result of initially-deferred gains becoming taxable. The Office of State Planning and Budgeting estimated this provision would not impact FY 2026 state revenues, but would reduce revenues by $20 million to $30 million in FY 2027 and by $40 million to $50 million in FY 2028. During the 2026 Legislative Session, Colorado passed legislation (House Bill 26-1289) to create a state addback for exempt federal Opportunity Zone gains starting in Tax Year 2027, unless those gains were invested in a QOF in Colorado. This avoids granting favorable tax treatment for investments made outside the state.

The OBBBA International Tax Changes

A significant component of the OBBBA involved changes to the taxation of international commerce and income earned abroad by multinational enterprises, including the following.

Foreign-Derived Intangible Income Amended, Foreign-Derived Deduction Eligible Income (FDDEI) Established (Potential for Significant Impact)
Description of Provision: The TCJA allowed a deduction for certain foreign source income, known as Foreign-Derived Intangible Income (FDII), arising from a trade or business within the United States and attributable to sales and services in foreign markets. This was meant to encourage multinational corporations to situate intellectual property in the U.S. and on-shore profits. The OBBBA renames FDII to FDDEI (Foreign-Derived Deduction Eligible Income) and streamlines the calculation. It expands the exceptions to Deduction Eligible Income (DEI) from six to eight categories and reduces the types of expenses considered when calculating total DEI. It reduces the deduction rate of FDDEI to 33.34 percent from 37.5 percent, meaning the new effective rate on FDDEI is 14 percent rather than 13.125 percent that was imposed under old FDII regime [26 USC 250(a),(b)].
Effective Date of Change: Applies to tax years beginning after 12/31/2025.
Potential State Impact: Colorado does not conform to this provision. House Bill 25B-1002 requires any deduction for foreign-derived deduction eligible income (FDDEI) pursuant to Section 250 of the Internal Revenue Code to be added back in determining Colorado taxable income. Legislative Council staff estimated that this addback would generate $35.6 million in FY 2026 and $72.2 million in FY 2027.

Global Intangible Low-Taxed Income Amended, Net CFC Tested Income (NCTI) Established

Description of Provision: The TCJA imposed a minimum tax on the income of U.S.-controlled foreign corporations in an attempt to reduce international profit shifting. Under the provision, corporations were required to include certain foreign source income known as Global Intangible Low-Taxed Income (GILTI) in their gross income. GILTI was determined by including a U.S.-based parent company's share of their controlled foreign corporations' (CFCs) aggregate income in the shareholder or parent's income to the extent that it exceeded a deemed 10 percent return on the CFC's tangible assets (known as the "qualified business asset investment" or QBAI reduction), excluding net tested losses. The term "deemed" refers to a return assumed by statute rather than one actually earned.

A deduction was allowed for 50 percent of this income for tax years beginning after December 31, 2017 and before January 1, 2026, at which point the deduction percentage was scheduled to be reduced from 50 percent to 37.5 percent.

The OBBBA replaces the GILTI regime and renames it NCTI ("Net CFC Tested Income"). The NCTI regime eliminates the exclusion from income for the deemed 10 percent return on tangible assets (QBAI) that was available under GILTI and reduces the deduction percentage for net CFC tested income (formerly known as GILTI) to 40 percent, resulting in a 12.6 percent effective tax rate [26 USC 951A(a)].

Other changes related to NCTI regime include:

- Extending subpart F and NCTI rules to foreign entities to address ownership structures that might otherwise avoid the tax (IRC subpart F attributes certain passive income earned by CFCs to the domestic shareholders, according to their interest in the CFC). [26 USC 951B].
- Increasing the net CFC tested income allowance from 80 percent to 90 percent, which ensures no residual U.S. tax would be owed on income subject to a 14 percent foreign tax rate. The provision disallows 10 percent of the deemed paid foreign tax credit for distributions of previously taxed net CFC income [26 USC 960(d)(1)].
- Limiting the expenses allocable to foreign-source income in the net CFC tested income (formerly known as GILTI) category to: (i) the §250 deduction for net CFC tested income and (ii) any other deduction that is "directly allocable" to net CFC tested income. No amount of interest expense or research and experimental expenditures are allocable to foreign-source net CFC tested income. Any deduction that would have otherwise been allocated to the net CFC tested income category but for this rule is allocated instead to U.S.-source income [26 USC 904(b)(5)].
- Providing that if a foreign corporation is a CFC at any time during a tax year, each U.S. shareholder that owns stock in such corporation during the CFC's year must include in gross income their pro rata share of the CFC's subpart F income. Additionally, ensuring that a U.S. shareholder of a CFC recognizes their pro rata share of the CFC's subpart F income, irrespective of ownership at the end of the tax year [26 USC 951(a)].

The JCT reported that the net effect of NCTI changes will increase revenues by tens of billions over the 10-year budget cycle, relative to the current policy baseline.

Effective Date of Change: Applies to tax years after 12/31/2025.

Potential State Impact: Colorado will automatically follow the federal government in switching from GILTI to NCTI, which could result in increased state tax revenues. However, some portion of GILTI, NCTI and FDII may be eliminated for Colorado income tax purposes by Colorado's state-level exclusion for foreign source income in Section 39-22-303(10) C.R.S. GILTI/NCTI is considered foreign source income for the purpose of this exclusion, but the extent to which the two interact depends on other variables, such as the amount of the foreign tax credit allowed to a taxpayer. CFCs incorporated in certain countries listed in Section 39-22-303(12)(b), C.R.S., are presumed to be for tax avoidance purposes. Statute [Sections 39-22-303(8)(b) and (8.5)(b)(I)(D), C.R.S.] requires corporations to include these CFCs in their Colorado combined report, which results in the CFCs' income being included in Colorado taxable income.

Look-Through Treatment of Payments Between Related Controlled Foreign Corporations Under the Foreign Personal Holding Company Rules

Description of Provision: According to the Congressional Research Service, regarding income earned by U.S. corporations' foreign subsidiaries, generally, "Income earned abroad by foreign-incorporated subsidiaries is taxed in full, not taxed at full rates, or not taxed at all. For passive income (such as interest income) and certain types of payments that can be easily manipulated to reduce foreign taxes, tax rules require this income earned by controlled foreign corporations (CFCs) to be taxed currently [i.e., in the same year it is earned]. A CFC is a foreign corporation controlled by U.S. shareholders owning more than 50 percent of vote or value. This income is referred to as Subpart F income, reflecting the part of the tax code where treatment is specified. Credits against the U.S. tax imposed are allowed for any foreign taxes paid on this income, and are applied on an overall basis... Other income earned abroad by CFCs is subject to the global intangible low-taxed income (GILTI) provision, which taxes this foreign-source income at half the corporate tax rate (10.5 percent), after allowing a deduction for a deemed return of 10 percent on tangible assets. Credits are allowed for 80 percent of foreign taxes paid."

Under the "look-through rule" (adopted in 2005 and subsequently extended several times, and scheduled to expire at the end of 2025), certain payments between related corporations can be excluded from income [26 USC 954(c)(6)]. According to the federal Joint Committee on Taxation, "dividends, interest…, rents, and royalties received or accrued by one CFC from a related CFC are not treated as foreign personal holding company income to the extent attributable or properly allocable to income of the payor that is neither subpart F income nor treated as ECI [Effectively Connected Income]." When a foreign person engages in a trade or business in the United States, all income from sources within the U.S. connected with the conduct of that business is considered "effectively connected income." The OBBBA permanently maintains this exemption.

According to the Congressional Research Service, "the main argument against the look-through rules… is that they undermine Subpart F's purpose, which is to prevent firms from using passive and easily shifted income to avoid taxation. The main argument for the provision is to allow firms the flexibility to redeploy earnings from one location to another without having U.S. tax consequences... An argument can also be made that in some cases…, the profit shifting is not harming the U.S. Treasury, but rather reducing taxes collected by foreign governments…"

The JCT estimated that this provision would reduce federal revenues by $534 million in FY 2026 and by $996 million in FY 2027, relative to the current law baseline.

Effective Date of Change: Applies to tax years beginning after 12/31/2025.

Potential State Impact: Colorado generally conforms to the treatment of subpart F income. We could not identify an estimate of the impact to the State from the extension of this provision, though it could reduce federal taxable income and state tax collections.

Reduction in IRS Funding/Administrative Capacity

The Federation of Tax Administrators has noted that states rely extensively on the IRS and its activities as part of and a complement to their enforcement and compliance programs; specifically, "While states devote substantial resources to the audit of corporation tax returns, their audit activities are focused primarily on verifying the apportionment of income across states, examining the taxpayer's treatment of certain types of transactions, and determining the membership of the unitary group if the state employs combined reporting. On the individual side, states also rely heavily on federal examinations and adjustments (particularly those involving the matching of information returns) as primary enforcement tools. In addition, states use federal income tax return data for a wide range of individual, independent enforcement programs…. States are also reliant on the federal information reporting mechanisms for state income tax administration. To a very considerable degree, states simply mirror federal requirements [and forms, formats, etc.] for third-party information reporting."

Over the course of 2025, IRS staffing was reduced by roughly 27 percent, from over 102,000 employees to approximately 74,000, amid funding reductions and the introduction of a deferred resignation program that allowed federal employees to voluntarily resign and receive pay through September 30, 2025. Some positions within the IRS experienced larger cuts than others. For example, IRS staffing levels within its Large Business and International Division were reduced by about 26 percent, while its Small Business/Self-Employed Division staffing levels fell 38 percent. Staffing levels with the Taxpayer Services Division declined by 21 percent. These cuts included revenue agents, who are the IRS workers who examine tax returns, perform audits, and advise on tax liability; revenue officers, who perform work related to collecting delinquent taxes and surveying for unreported taxes; and tax examiners, who perform work related to processing tax returns, managing accounts, collecting taxes and/or obtaining tax returns, computing or verifying tax, and determining proper tax liabilities. The Treasury Inspector General has noted that Colorado has been among the states with the highest percentage of employee separations (i.e., terminations or deferred resignations) from the IRS.

Research shows that IRS audits have a strong return on investment ratio, and that a reduction in tax enforcement funding can result in significantly more lost revenue. One recent academic estimate prepared by Boning et al. and published by the Quarterly Journal of Economics noted that, on average, $1 in audit spending initially raises $2.17 in revenue, with audits of taxpayers in the top 0.1 percent of income yielding a return of 6.3:1. There is an additional indirect deterrence effect of audits on future revenues that produces at least three times more revenue than the initial audit. Based on these results, the Institute on Taxation and Economic Policy estimates that a $2.84 billion cut to audits could theoretically result in tens of billions in foregone revenue.

Many state tax officials have expressed concern about the impacts of a reduction in the IRS's capacity. In an interview with Bloomberg Law, Utah's Commissioner of Revenue stated that: "Most states simply adopt the fundamental figure of federal taxable income to begin their analysis of taxpayers' state income tax obligations... They deploy more than 90% of their audit and collection resources to factors below that line. Any disruption at the IRS in calculations and compliance processes could filter down to the states… 'It is conceivable that reductions in force at the federal level could affect the revenues flowing to the states. It could affect it in enforcement. It could affect it in compliance'."

Colorado Department of Revenue staff reported to us that it relies heavily on federal tax information in evaluating the accuracy of Colorado returns. Therefore, to the extent that changes in IRS examination levels reduce the examination of taxpayers subject to Colorado income tax, those changes will directly affect Colorado income tax collections. Department staff also noted that reductions in IRS examination levels could impact Colorado income tax collections if they change taxpayers' perceptions of enforcement risk. Taxpayers may be more aggressive in their tax avoidance efforts if they believe the risk of IRS examination is lower, and this could indirectly impact Colorado. However, this is not something the Department can quantify. To date, the principal impacts on the Department have stemmed from the inability of the IRS to rectify prior processing backlogs that arose during the pandemic. These backlogs have delayed data releases from the IRS, which have, in turn, delayed the Department's ability to analyze state returns and produce statistical reports that rely on this data. (Note, this delay has also affected the OSA's ability to provide more up-to-date figures on federal deductions taken by Colorado taxpayers in this report).

Appendix A

Income Items Explicitly Included in Federal Gross Income

This appendix provides a list of the types of items that are explicitly included in gross income per federal law. Additionally, in the list, we indicate when Colorado has enacted legislation to deviate from the federal tax treatment of certain types of income and the revenue impact of doing so, when data were available.

- **Compensation for services including fees, commissions, and fringe benefits;** Colorado law deviates from federal treatment of compensation in a few instances. Specifically:
    - **Certain employer-provided benefits**—Colorado statute [Sections 39-22-104(4)(o) and (bb), C.R.S.] allows individual taxpayers to deduct contributions made to certain accounts on their behalf by their employer from federal taxable income when calculating Colorado taxable income. Specifically, individual taxpayers may deduct amounts received by their employer as matching contributions to their adult learners trust or savings account with CollegeInvest. For Tax Years 2024 through 2026, individuals may also deduct any employer contribution made to their qualifying home savings account that is included in federal taxable income. These contributions are likely considered taxable fringe benefits for federal tax purposes.
    - **Military service members who reacquire Colorado residency**—Colorado statute [Section 39-22-104(4)(u), C.R.S.] allows a military service member who is a Colorado resident to claim a deduction for any compensation they receive for active duty military service that is included in their federal taxable income if (1) the service member's home of record is Colorado, (2) while in the military, the service member acquired legal residence in a state other than Colorado, and (3) and the service member subsequently reacquired Colorado residency. According to Department of Revenue data, in Tax Year 2023, this deduction was claimed on 46 returns for a total revenue impact of about $205,000 to the State.
    - **Military Family Relief Fund grants**—Colorado statute [Section 39-22-104(4)(p), C.R.S.] allows Colorado taxpayers to deduct any amount received as a grant from the Military Family Relief Fund from their federal taxable income when calculating Colorado taxable income, to the extent it is included in federal taxable income. Based on our review of this deduction in 2022, it appears that its revenue impact is small, although it is unclear how many taxpayers may have used it.
- **Property transferred in connection with performance of services (e.g., restricted stock plans).**
- **Gross income derived from business.**

- **Gains from dealings in property (e.g., capital gains)**. Capital gains are typically taxed at lower rates than sources of ordinary income, such as compensation. According to Internal Revenue Service guidance, "Almost everything [a taxpayer] own[s] and use[s] for personal or investment purposes is a capital asset. Examples of capital assets include a home, personal-use items like household furnishings, and stocks or bonds held as investments. When [a taxpayer] sell[s] a capital asset, the difference between the adjusted basis in the asset and the amount…realized from the sale is a capital gain or a capital loss. Generally, an asset's basis is its cost to the owner, but if [the taxpayer] received the asset as a gift or inheritance [different rules apply]." If the taxpayer sells the asset for more than its adjusted basis, it is a capital gain. The federal capital gain tax rates generally range from 0 to 20 percent, depending on the taxpayer's taxable income. It is important to note that even though capital gains are taxed at a lower rate than ordinary income, the amount of the capital gain is generally included in federal taxable income; the tax benefit comes from a lower tax rate applied to the capital gain at the federal level. Colorado does not tax capital gains at a separate rate, so for state tax purposes, capital gains are treated the same as other forms of income. Colorado statute [Section 39-22-518, C.R.S.] allows certain taxpayers to deduct certain capital gains included in federal taxable income when calculating their Colorado taxable income. Beginning in Tax Year 2022, the deduction is only allowed for capital gains recognized by qualifying farmers from the sale of agricultural real property that the taxpayer acquired on or after May 9, 1994, but before June 4, 2009. According to Department of Revenue data, in Tax Year 2023, this deduction was claimed on 232 returns for a total revenue impact of about $610,400 to the State.

- **Interest earnings.** Colorado statute [Sections 39-22-104(4)(a) and 304(3)(a), C.R.S.] allows both individual and corporate taxpayers to deduct from their federal taxable income when calculating Colorado taxable income any interest income on obligations of the United States and its possessions (to the extent included in federal taxable income). Additionally, corporations may deduct any interest or dividend income on obligations or securities of any authority, commission, or instrumentality of the United States to the extent it is included in federal taxable income but exempt from state income taxes under laws of the United States [Section 39-22-304(3)(b), C.R.S.]. According to Department of Revenue data, in Tax Year 2023, this deduction was claimed on 125,453 individual returns for a total revenue impact of about $45.1 million to the State. In that same year, the deduction was claimed on 1,564 corporate returns for a total revenue impact of about $2.4 billion to the State.

- **Rents.**

- **Royalties.**

- **Dividends.**

- **Annuities.**

- **Income from life insurance and endowment contracts.**

- **Pensions and some Social Security benefits.** Colorado allows two deductions from federal taxable income related to pension and Social Security benefits. Specifically,
  - **Social Security and pension income.** Colorado statute [Section 39-22-104(4)(f), C.R.S.] allows some individuals who have Social Security and some pension income that is included in federal taxable income to deduct this income from federal taxable income when calculating Colorado taxable income. According to Department of Revenue data, in Tax Year 2023, this deduction was claimed on 573,941 returns for a total revenue impact of about $629.7 million to the State.
  - **Military retirement benefits.** Statute [Section 39-22-104(4)(y), C.R.S.] also allows members of the United States uniformed services, including members of the armed forces (i.e., Amy, Navy, Air Force, Marine Corps, Space Force, Coast Guard) and members of the Commissioned Corps of the National Oceanic and Atmospheric Administration and Public Health Service, who are under 55 years of age to deduct up to $15,000 of the military retirement benefits that are included in their federal taxable income. If they are 55 years of age or older, they can claim the regular pension deduction mentioned above. According to Department of Revenue data, in Tax Year 2023, the military retirement deduction was claimed on 6,146 returns for a total revenue impact of about $4.0 million to the State.
- **Income from discharge of indebtedness.**
- **Distributive share of partnership gross income.**
- **Income in respect of a decedent.**
- **Income from interest in an estate or trust.**
- **Prizes and awards.** Federal law provides an exception to this in 26 USC 74(d) for taxpayers with $1 million or less in federal adjusted gross income who win medals at the Olympic or Paralympic Games. Those taxpayers are allowed to exclude from gross income the value of the medal as well as any prize money received from the United States Olympic Committee. Colorado generally conforms to this provision of the IRC but also allows taxpayers to deduct prize money given by any sport-specific national governing body or Paralympic sport organization in which the prize is connected with winning the medal [Section 39-22-104(4)(x), C.R.S.].
- **Unemployment compensation.**
- **Some group-term life insurance purchased by employers for employees.**
- **Reimbursement for expenses of moving from one residence to another due to employment.**
- **Transfers of appreciated property to political organizations.**
- **Certain federal tax credits (e.g., alcohol and biodiesel fuels credits).**

Appendix B

Income Items Explicitly Excluded from Federal Gross Income

This appendix provides a list of types of items that are explicitly excluded from federal gross income with brief descriptions. Additionally, in the list, we indicate when Colorado has enacted legislation to deviate from the federal tax treatment of certain exclusions from income and the revenue impact of doing so, when data were available.

Income Item	Description
Certain Death Benefits [26 USC 101]	In general, life insurance proceeds that a beneficiary receives due to the death of the insured person are excluded from gross income. Additionally, gross income does not include any amount paid as a survivor annuity on account of the death of a public safety officer provided that certain conditions are met.
Gifts and Inheritance [26 USC 102]	In general, gross income does not include the value of property acquired by gift, bequest, devise, or inheritance. However, gifts received by employees from their employers are subject to tax.
Interest on State and Local Bonds [26 USC 103]	Interest on state and local bonds, including the District of Columbia and possessions of the United States, is excluded from gross income, with a few exceptions such as private activity bonds. Colorado does not fully conform to this provision of the IRC. Colorado taxes non-Colorado state and local bond interest. Sections 39-22-104(3)(b) and 304(2)(b), C.R.S., require that both individual and corporate taxpayers add back any interest on state and local bonds other than interest from State of Colorado or any political subdivision thereof to federal taxable income when calculating Colorado taxable income.
Compensation for Injuries or Sickness [26 USC 104]	In general, the following amounts are excluded from gross income: amounts received under worker's compensation acts as compensation for personal injuries or sickness, amounts received through accident or health insurance for personal injuries or sickness, and damages (except punitive damages) received on account of personal injuries or physical sickness from settlements from lawsuits and agreements. However, IRS guidance provides that the facts and circumstances surrounding each settlement payment must be considered because not all amounts received from settlements are exempt from taxes.
Amounts Received Under Accident and Health Plans [26 USC 105(b)]	Amounts received by the taxpayer as reimbursement for medical care of themselves, their spouse, their dependents, or their child under 27 years old are excluded from gross income. Medical care may include a chronic or acute condition or illness but does not include reimbursement for items used for general health (e.g., dietary supplements). An example of this kind of arrangement is an employer flexible spending account (FSA) in which the employer reimburses the employee for expenses for medical care.

Income Item	Description
Contributions by Employer to Accident and Health Insurance Plans [26 USC 106(a) and (d)]	In general, the amount of an employee's health or accident insurance plan premium that is paid for by the employer is excluded from the employee's gross income. Additionally, employer contributions to employees' health savings accounts (HSAs), subject to a limit, are not included in the employees' gross income if the employee is on a high deductible insurance plan.
Income from Discharge of Indebtedness [26 USC 108]	Certain discharges of indebtedness are excluded from gross income, including if the discharge occurred in a Title 11 bankruptcy case, when the taxpayer is insolvent, and when the discharge is qualified farm indebtedness, when the indebtedness is qualified real property indebtedness (but not for C corporations), and when the indebtedness discharged is qualified principal resident indebtedness that is discharged before January 1, 2026.
Improvements by Lessee on Lessor's Property [26 USC 109]	Gross income does not include income (other than rent) derived by a lessor of real property on the termination of a lease, representing the value of such property attributable to buildings erected or other improvements made by the lessee.
Qualified Lessee Construction Allowances for Short-term Leases of Retail Space [26 USC 110(a)]	Gross income of a lessee does not include any amount received in cash or as a rent reduction by a lessee from a lessor under a short-term lease (i.e., 15 years or less) of retail space and for the purposes of constructing or improving qualified long-term real property for use in the lessee's trade or business as long as the lessee's trade or business is selling tangible personal property or services to the general public. The exclusion is only allowed to the extent that the amount does not exceed the amount expended by the lessee for the construction or improvement.
Recovery of Tax Benefit Items [26 USC 111]	Gross income does not include income attributable to the recovery of any amount deducted or taken as a credit in a prior tax year to the extent that it did not reduce the amount of income tax imposed. Although this section applies to a variety of deductions and credits, the most common application is for state and local tax refunds.
Certain Combat Zone Pay [26 USC 112]	Compensation received for active service in the United States Armed Forces for any month in which the member served in a combat zone or was hospitalized as a result of wounds, disease, or injury incurred while serving in a combat zone (for up to 2 years) is excluded. The amount excluded depends on the rank of the member.
Qualified Scholarships [26 USC 117]	Any amount received as a qualified scholarship by an individual who is a candidate for a degree at an educational organization that normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of students in attendance at the place where its educational activities are regularly carried on is excluded from gross income. A qualified scholarship is the amount received as a scholarship or fellowship grant that is used for tuition, fees, books, supplies, and equipment required for enrollment/attendance at the institution and for classes.
Contributions to the Capital of a Corporation [26 USC 118]	In the case of a corporation, any contribution of money or property to the capital of the taxpayer is excluded from gross income; if a corporation requires additional funds for conducting its business and obtains such funds through voluntary pro rata payments by its shareholders, the amounts so received being credited to its surplus account or to a special account, such amounts do not constitute income, although there is no increase in the outstanding shares of stock of the corporation. The exclusion also applies to contributions to capital made by persons other than shareholders. For example, the exclusion applies to the value of land or other property contributed to a corporation by a governmental unit or by a civic group for the purpose of inducing the corporation to locate its business in a particular community, or for the purpose of enabling the corporation to expand its operating facilities.

Income Item	Description
Meals or Lodging Furnished for the Convenience of Employer [26 USC 119]	In general, the value of any meals or lodging furnished to employees, their spouse, or their dependents by or on behalf of their employer for the convenience of the employer are excluded from gross income. The meals must be furnished on the business premises of the employer and the employee must be required to accept the lodging on the business premises of the employer as a condition of employment in order to qualify.
Exclusion of Gain from Sale of Principal Residence [26 USC 121]	Up to $250,000 ($500,000 if married filing a joint return) of the gain from the sale of the taxpayer's principal residence is excluded from gross income. To qualify, for the 5-year period ending on the date of the sale, the property had to have been owned and used by the taxpayer for at least 2 of those years.
Amounts Received Under Insurance Contracts for Certain Living Expenses [26 USC 123]	When an individual's principal residence is damaged or destroyed by a casualty or their access to the principal residence is restricted by the government because of the occurrence or threat of a casualty, the individual's gross income does not include amounts received under an insurance contract, which are paid to compensate or reimburse the individual for living expenses incurred for themselves and members of their household resulting from the loss of use or occupancy of the residence. The exclusion is limited to the amount of expenses incurred above the normal living expenses that would have been incurred by the individual and their household members during the period.
Cafeteria Plans [26 USC 125]	According to Bloomberg Law, "A cafeteria plan is a type of employee benefit plan that permits each participating employee of the employer to choose among two or more benefits consisting of cash and qualified benefits. In making this choice, the employee may obtain nontaxable benefits by foregoing taxable cash compensation." Benefits/plans include health savings accounts, flexible savings accounts, health insurance premiums, and dependent care assistance programs. In order for an employer to sponsor a Section 125 plan, the business must employ an average of 100 or fewer employees during either of the 2 preceding years.
Educational Assistance Programs [26 USC 127]	Gross income of an employee does not include amounts paid or expenses incurred by an employer for educational assistance to the employee if the assistance is for an eligible program, or for principal or interest payments on qualified education loans made by the employer on behalf of the employee. The exclusion is limited to $5,250 per calendar year, adjusted for inflation annually in tax years after 2026.
Employer Contributions to Trump Accounts [26 USC 128]	Gross income of an employee does not include amounts paid by the employer as a contribution to the Trump account of such employee or of any dependent of such employee if the amounts are paid or incurred pursuant to the Trump account contribution program. The amount that may be excluded shall not exceed $2,500 in 2026. (The limitation is adjusted for inflation beginning in 2027.)
Dependent Care Assistance Programs [26 USC 129]	Gross income of an employee does not include amounts paid or incurred by the employer for dependent care assistance provided to such employee if the assistance is furnished pursuant to a dependent care assistance program. The exclusion is generally limited to $7,500 per year.
Certain Foster Care Payments [26 USC 131]	Amounts received by a foster care provider as qualified foster care payments are excluded from gross income.
Certain Fringe Benefits [26 USC 132]	Gross income does not include certain, specified fringe benefits, including no-additional cost services, qualified employee discounts, working condition fringe, de minimus fringe, qualified transportation fringe, qualified moving expense reimbursement fringe for certain military and intelligence community personnel, qualified retirement planning services, and qualified military base realignment and closure fringe. Several of these are subject to limits.

Income Item	Description
Income from United States Savings Bonds Used to Pay Higher Education Tuition and Fees [26 USC 135]	Income from qualified United States savings bonds may be excluded from gross income provided that certain conditions are met. The bonds must be series EE or I U.S. savings bonds issued after 1989 that were issued to the taxpayer when they were at least 24 years old. The bond has to have been cashed in the year in which qualified higher expenses were incurred. There are income restrictions, which are adjusted annually, on who is allowed to claim this exclusion.
Energy Conservation Subsidies Provided by Public Utilities [26 USC 136]	Gross income does not include the value of any subsidy (e.g., a rebate) provided directly or indirectly by a public utility to a customer for the purchase or installation of installations or modifications designed to reduce consumption of electricity or natural gas, or improve the management of energy demand, of a house, apartment, condominium, mobile home, boat, or similar property.
Adoption Assistance Programs [26 USC 137]	In general, gross income of an employee does not include amounts paid or expenses incurred by an employer for qualified adoption expenses if the amounts are provided pursuant to an adoption assistance program. The exclusion is subject to a $10,000 cap, which is indexed for inflation. There is a higher cap if the adoption is of a child with special needs. The exclusion amount is reduced for taxpayers with and adjusted gross income over a certain amount.
Medicare Advantage MSA [26 USC 138]	Gross income does not include any payment to a Medicare Advantage medical savings account (MSA) of an individual by the Secretary of Health and Human Services under certain provisions of the Social Security Act [42 USC 1395w-21 et seq].
Disaster Relief Payments [26 USC 139]	In general, amounts received by individuals as qualified disaster relief payments are excluded from gross income. Qualified disasters are disasters resulting from terrorism or a military action, federally declared disasters, or an accident that the Secretary of the Treasury determines to be catastrophic. Qualified disaster relief payments are amounts provided to an individual to reimburse or pay for qualifying expenses incurred as a result of a qualified disaster.
Benefits Provided to Volunteer Firefighters and Emergency Medical Responders [26 USC 139B]	Volunteer firefighters and emergency medical responders can exclude from their gross income any qualified state and local tax benefit (i.e., reductions or rebates of state and local income and property taxes) and payments from state and local governments of up to $50 per month.
Certain Disability-related First Responder Retirement Payments [26 USC 139C]	Qualified first responders, including law enforcement officers, firefighters, paramedics, and emergency medical technicians, may exclude a portion of their disability retirement payments from gross income.
Certain Amounts Received by Wrongfully Incarcerated Individuals [26 USC 139F]	Gross income for wrongfully incarcerated individuals does not include any civil damages, restitution, or other monetary award relating to the incarceration of the individual for a criminal offense under federal or state law (including any criminal offense arising from the same source of conduct as that criminal offense) for which the individual was convicted. Colorado generally conforms to this provision of the IRC, but also allows a deduction to be claimed if the compensation or damages is provided to an immediate family member of the exonerated person [Section 39-22-104(4)(q), C.R.S.].
Certain Contributions to Trump Accounts [26 USC 139J]	Gross income of an account beneficiary does not include any qualified general contribution to a Trump account of the beneficiary. Earnings from Trump accounts, however, are subject to tax when distributed, similar to a traditional IRA. Contributions to Trump accounts cannot be made before July 4, 2026.

Income Item	Description
Scholarships for Qualified Elementary or Secondary Education Expenses of Eligible Students [139K]	Effective Dec. 31, 2026, gross income does not include any amounts provided to an individual or dependent of an individual pursuant to a scholarship for qualified elementary or secondary education expenses of an eligible student provided by a scholarship granting organization.
Interest on Loans Secured by Rural or Agricultural Real Property [139L]	Gross income does not include 25 percent of the interest received by a qualified lender on any qualified real estate loan made after July 4, 2025.
Qualified Tuition Program Distributions [26 USC 529(c)]	Distributions from qualified tuition programs (often referred to as "Section 529 plans") are generally excluded from gross income when the distributions are used to pay for qualified elementary and secondary tuition or qualified higher education and postsecondary expenses for the beneficiary of the account. Additionally, up to $10,000 per year may be used for tuition expenses for the account beneficiary's attendance at an elementary or secondary public, private, or religious school. After December 31, 2023, the beneficiary of a qualified tuition program may roll over some of a distribution to a Roth IRA, subject to the Roth IRA annual contribution limit and a $35,000 lifetime limit. The rollover must be paid through a direct trustee-to-trustee transfer, and the account must have been opened for at least 15 years to qualify for the tax-free Roth IRA rollover. Colorado generally conforms to the federal tax treatment of distributions from Section 529 plans when they are used to pay for qualified higher education expenses. However, if any distribution or withdrawal made from a qualified state tuition program account is used to pay for elementary or secondary education expenses, the account holder must add that amount back to their federal taxable income when calculating Colorado taxable income. Additionally, since Colorado statute only allows the deduction for higher education expenses, amounts in a 529 account that are rolled over into a Roth IRA must also be added back to federal taxable income when calculating Colorado taxable income.
Qualified ABLE Account Distributions [26 USC 529A(c)]	ABLE accounts operate similarly to qualified tuition programs authorized under 26 USC 529, except the funds are used to pay for qualified disability expenses for people with disabilities whose disabilities occurred before age 46. When the funds are used to pay for eligible expenses for a beneficiary with a disability, the distributions are excluded from gross income. According to IRS guidance, the following type of expenses are eligible: education, housing, transportation, employment training and support, assistive technology, personal support services, health, prevention and wellness, financial management, administrative services, legal fees, expenses for oversight and monitoring, and funeral and burial expenses. ABLE accounts are also subject to different limits than qualified tuition programs. Federal law imposes a limit on the total amount of contributions that can be made to an ABLE account from all contributors during the year. In 2026, the contribution limit is $20,000.
Trump Accounts [26 USC 530A]	Trump accounts are savings vehicles that operate similar to an individual retirement account that are created for the exclusive benefit of an individual under age 18 with a valid Social Security number. Contributions to these accounts are excluded from the gross income of the account beneficiary. The aggregate amount of contributions to such an account cannot exceed $5,000 in a taxable year. This limit is adjusted for inflation annually starting in tax years after 2027.

Income Item	Description
Foreign Earned Income [26 USC 911]	An individual whose tax home is in a foreign country, and whom is either a citizen of the United States and a resident of another country or a United States citizen or resident who spent the majority of the tax year in a foreign country, may be eligible to exclude a portion of their foreign earned income (i.e., wages, salaries, or professional fees) from gross income. In Tax Year 2026, the maximum exclusion amount is $132,900 per person.

Source: Office of the State Auditor analysis of federal laws, Internal Revenue Service taxpayer guidance documents, Internal Revenue Service data, Colorado laws, Colorado Department of Revenue taxpayer guidance documents, Colorado Department of Revenue data, and Bloomberg Law documents.

Appendix C

Above-the-Line Deductions

This appendix provides a list of above-the-line deductions (with descriptions and claims data, when available) that can be taken from federal gross income to determine federal adjusted gross income. Additionally, we indicate when Colorado has enacted legislation to deviate from the federal tax treatment of above-the-line deductions and the revenue impact of doing so, when data were available.

Deduction	Description
Trade and Business Deductions [26 USC 62(a)(1), 26 USC 1 et seq but not including 26 USC 211 through 223]	The taxpayer may claim deductions for trade or business expenses that are attributable to a trade or business that is carried on by the taxpayer, as long as the trade or business does not consist of the performance of services by the taxpayer as an employee. This includes, for example, ordinary and necessary business expenses such as salaries and other compensation for services, traveling expenses, rentals or other payments for use of property the business does not own, taxes paid by the business, business interest, and business bad debts. An individual may have trade and business expenses if they own and operate a business, for example, as a sole proprietor. Trade and business expenses allowed in 26 USC 162 are discussed more in depth in Appendix E. Taxpayers may not deduct any expenses incurred in carrying on any trade or business if such trade or business (or the activities which comprise such trade or business) consists of trafficking in controlled substances (within the meaning of schedule I and II of the Controlled Substances Act) which is prohibited by Federal law or the law of any state in which such trade or business is conducted [26 USC 280E]. In certain circumstances, Colorado law deviates from federal tax treatment of trade and business deductions. Specifically: • Colorado statutes [Section 39-22-104(3)(i) and 529, C.R.S.] require that companies that deducted on their federal returns wages or remuneration paid to unauthorized aliens in excess of $600 pursuant to 26 USC 162(a)(1) to add back the amount deducted on their federal return, subject to a few exceptions. • Under the IRC, businesses may be able to deduct 50 percent of business meal expenses. Note, however, for Tax Years 2024 through 2030, Colorado does not conform to this provision of the IRC and requires that individuals who claimed a deduction for business meals on their federal return add the amount claimed back when calculating their Colorado taxable income [Section 39-22-104(3)(s)(I), C.R.S.]. • To the extent that a taxpayer claimed a deduction on their federal return for expenses or payments to a club that has a policy to restrict membership on the basis of sex, sexual orientation, gender identity, gender expression, marital status, race, creed, religion, color, ancestry, or national origin, the taxpayer must add those back to their federal taxable income when calculating Colorado taxable income [Section 39-22-

	104(3)(e)(I), C.R.S.]. • Statutes [Section 39-22-104(4)(r) and (r.5), C.R.S.] allow individuals licensed under the Colorado Marijuana Code or Colorado Natural Medicine Code to deduct amounts equal to expenditures that would be eligible to be claimed as a deduction under federal law except that the deduction is disallowed under Section 280E because marijuana/natural medicine are considered controlled substances under federal law. According to statute [Section 44-50-103(13)(a), C.R.S.], natural medicine is psilocybin or psilocin. According to Department of Revenue data, in Tax Year 2023, the marijuana business expense deduction was claimed on 263 individual returns for a total revenue impact of about $1.6 million to the State, and on 148 corporate returns for a revenue impact of $3.8 million. The Department does not have data available for the natural medicine expenses deduction since that deduction did not go into effect until Tax Year 2024.
Reimbursed Expenses of Employees [26 USC 62(a)(2)(A)]	The taxpayer (employee) may claim a deduction for certain trade or business expenses paid or incurred by the taxpayer (employee) in connection with the performance of services as an employee under a reimbursement or other expense allowance arrangement with their employer, to the extent that those reimbursements from their employer were included in their gross income.
Certain Expenses of Performing Artists [26 USC 62(a)(2)(B)]	A taxpayer who is a qualified performing artist may claim a deduction for trade or business expenses (e.g., traveling expenses, rentals of property) paid or incurred in connection with the performance of services in the performing arts as an employee.
Certain Expenses of Officials [26 USC 62(a)(2)(C)]	A taxpayer who is an official may claim a deduction for trade or business expenses (e.g., traveling expenses, rentals of property) paid or incurred with respect to services performed as in their capacity as an official of an employee of a state or political subdivision if they are in a position that is compensated wholly or partially on a fee basis.
Certain Expenses of Elementary and Secondary School Teachers [26 USC 62(a)(2)(D)]	A taxpayer who is an eligible elementary or secondary school teacher may deduct expenses paid or incurred for professional development related to the curriculum the educator provides or for books, supplies, computer and other equipment, and supplementary materials used by the educator in their classroom, up to a statutory cap, which is adjusted for inflation. In 2026, the amount is $350. If two eligible educators file a joint return, they may each claim up to the cap. According to Internal Revenue Service Statistics of Income data for federal returns filed by taxpayers with a Colorado address, in Tax Year 2022, which was the most recent year of data available, this deduction was claimed on about 59,000 returns for a total of about $17.1 million in federal deductions. Based on Colorado's 4.4 percent tax rate, we estimate that this deduction could have reduced state revenue by about $751,100 in Tax Year 2022.
Certain Expenses of Members of Reserve Components of the Armed Forces of the United States [26 USC 62(a)(2)(E)]	A taxpayer who is a member of the National Guard or is a military reservist may deduct certain expenses (e.g., travel) when they travel more than 100 miles away from home for work in their capacity as a member of the National Guard or military reservist. According to Department of Revenue data, in Tax Year 2021, this deduction was claimed on 2,112 federal returns filed by full-year Colorado residents for a total of about $10.6 million in deductions. Based on Colorado's 4.5 percent tax rate in Tax Year 2021, we estimate that this deduction could have reduced state revenue by about $476,900.

Deduction	Description
Losses from Sale or Exchange of Property [26 USC 62(a)(3)]	An individual taxpayer may deduct a loss incurred from the sale or exchange of property when the loss is incurred in a trade or business or in a transaction that is entered into for profit, though not connected with a trade or business. Additionally, individuals may deduct capital losses to the extent of personal gains plus an additional $3,000 that they can use to offset other income.
Deductions Attributable to Rents and Royalties [26 USC 62(a)(4), 26 USC 161 through 198, 26 USC 212, 26 USC 611]	An individual may deduct trade or business expenses, expenses for the production of income, and depletion that are attributable to property held for the production of rents or royalties. Examples of this kind of property are rental real estate and oil and gas producing property.
Certain Deductions of Life Tenants and Income Beneficiaries of Property [26 USC 62(a)(5), 26 USC 167, 26 USC 611]	If the taxpayer is a life tenant of property (i.e., they have the right to use the property during their lifetime but do not own it), the income beneficiary of property held in a trust, or an heir, legatee, or devisee of an estate, they are allowed to claim a deduction for depreciation or depletion for the property.
Pension, Profit-sharing, and Annuity Plans of Self-employed Individuals [26 USC 62(a)(6), 26 USC 401(c)(1), 26 USC 404]	Any deduction allowed under 26 USC 404 (relating to contributions to pension, profit-sharing, annuity, or other qualified retirement plan) for a self-employed taxpayer is allowed from gross income.
Retirement Savings [26 USC 62(a)(7), 26 USC 219]	An individual taxpayer may deduct amounts contributed to qualifying individual retirement accounts or individual retirement annuities.
Penalties Forfeited Because of Premature Withdrawal of Funds from Time Savings Accounts or Deposits [26 USC 62(a)(9), 26 USC 165]	An individual taxpayer is allowed to claim a deduction for losses (as allowed under 26 USC 165) incurred in any transaction entered into for profit, though not connected with a trade or business, to the extent that such losses include amounts forfeited to a bank, mutual savings bank, savings and loan association, building and loan association, cooperative bank or homestead association as a penalty for premature withdrawal of funds from a time savings account, certificate of deposit, or similar class of deposit.
Reforestation Expenses [26 USC 62(a)(11), 26 USC 194]	Eligible individual taxpayers are allowed to deduct up to $10,000 (with amounts over $10,000 allowed to be amortized) for certain reforestation expenses that result in the establishment of commercial timber.
Certain Required Repayments of Supplemental Unemployment Compensation Benefits [26 USC 62(a)(12), 26 USC 165, 26 USC 501(c)]	Certain repayments of supplemental unemployment compensation benefits can be deducted.
Jury Duty Pay Remitted to Employer [26 USC 62(a)(13)	An individual who remits any portion of their jury pay to their employer in exchange for their employer continuing to pay them during their jury service is allowed to deduct the amount of the jury pay remitted to their employer.

Deduction	Description
Moving Expenses [26 USC 62(a)(15), 26 USC 217]	A taxpayer who moves for work (either for an employer or for self-employment at a new location) may deduct reasonable expenses relating to (1) moving their household goods and personal effects from the former residence to the new residence, and (2) traveling from the former residence to the new residence. To qualify, the taxpayer's new principal place of work must be at least 50 miles greater than the distance between their former residence and former principal place of work or if they had no former place of work, then the new principal place of work must be at least 50 miles from their former residence. Additionally, in the 12-month period immediately following arrival in the new principal place of work, the taxpayer must be employed full time by an employer or in the 24-month period immediately following arrival in the new location, the taxpayer must be self-employed on a full-time basis. This deduction is only available for members of the U.S. Armed Forces and members of the intelligence community who move pursuant to a military order incident to a permanent change of station.
Archer MSAs [26 USC 62(a)(16), 26 USC 220]	Subject to limitations, taxpayers may deduct amounts contributed to Archer medical savings accounts (MSAs). According to IRS guidance, "Archer MSAs were created to help self-employed individuals and employees of certain small employers meet the medical care costs of the account holder, the account holder's spouse, or the account holder's dependent(s). After 2007, you can't be treated as an eligible individual for Archer MSA purposes unless: 1. You were an active participant for any tax year ending before 2008, or 2. You became an active participant for a tax year ending after 2007 by reason of coverage under a high deductible health plan (HDHP) of an Archer MSA participating employer."
Interest on Education Loans [26 USC 62(a)(17), 26 USC 221]	Individual taxpayers may deduct the lesser of the amount of interest paid on eligible higher education loans or $2,500. The deductible amount is phased out and eventually eliminated as taxpayer adjusted gross income increases. According to IRS Statistics of Income data for federal returns filed by taxpayers with a Colorado address, in Tax Year 2022, which was the most recent year of data available, this deduction was claimed on about 84,000 returns for a total of about $75.4 million in federal deductions. Based on the State's 4.4 percent income tax rate, we estimate that this deduction could have reduced state tax revenue by about $3.3 million in Tax Year 2022.
Health Savings Accounts [26 USC 62(a)(19), 26 USC 223]	In general, an eligible taxpayer may deduct amounts contributed to a health savings account (HSA). According to IRS guidance, "An HSA is a tax-exempt trust or custodial account you set up with a qualified HSA trustee to pay or reimburse certain medical expenses you incur. You must be an eligible individual to contribute to an HSA… To be an eligible individual and qualify for an HSA contribution, you must meet the following requirements. You are covered under a high deductible health plan (HDHP)… on the first day of the month. You have no other health coverage except what is permitted under other health coverage. You aren't enrolled in Medicare. You can't be claimed as a dependent on someone else's … tax return." There are limits on the amounts that may be contributed annually to HSAs. In 2026, the limit for individuals with self-only coverage was $4,400 and $8,750 for family coverage. Individuals who are at least 55 years of age can contribute an additional $1,000. According to Department of Revenue data, in Tax Year 2021, this deduction was claimed on 58,412 federal returns filed by full-year Colorado residents for a total of about $203.4 million in deductions. Based on the State's 4.5 percent income tax rate in 2021 we estimate that this deduction could have reduced state tax revenue by about $9.2 million in Tax Year 2021.

Deduction	Description
Costs Involving Discrimination Suits [26 USC 62(a)(20)]	According to Bloomberg Law, taxpayers are allowed to claim a deduction for “attorney fees and court costs that satisfy two conditions…First, the fees and costs must be paid by, or on behalf of, the taxpayer. Second, they must be paid in connection with any action involving a claim of unlawful discrimination, a claim of a violation of 31 U.S.C. 3721 et seq, or a claim made under 1862(b)(3)(A) of the Social Security Act. Only the portion of the fees and costs that do not exceed the amount includible in the taxpayer’s gross income for the tax year on account of a judgment or settlement…resulting from the claim are allowable in computing adjusted gross income.” There are various federal acts that a claim of unlawful discrimination can fall under, including, but not limited to the Civil Rights Act of 1991 and certain sections of the Civil Rights Act of 1964, the National Labor Relations Act, the Fair Labor Standards Act of 1938, certain sections of the Family and Medical Leave Act of 1993, certain sections of the Fair Housing Act, and certain sections of the Americans with Disabilities Act of 1990.
Attorneys’ Fees Relating to Awards to Whistleblowers [26 USC 62(a)(21)]	An individual may deduct attorney fees and court costs paid by, or on behalf of, the taxpayer in connection with an award related to being a whistleblower.
Casualty and Losses [26 USC 165(h)(4)]	In general, individuals may claim a deduction for the loss of property arising from fire, storm, shipwreck, or other casualty, or from theft. The loss may only be claimed to the extent of a personal casualty gain, which is a gain from any involuntary conversion of property arising from fire, storm, shipwreck, or other casualty, or from theft. A personal casualty gain could occur when insurance or other reimbursement for a loss of property exceeds the taxpayer’s adjusted basis in the property. Additionally, the loss is only allowed to the extent that each casualty or theft loss exceeds $100. For tax years beginning after 2017, casualty and theft losses of property not connected with a trade or business or transaction entered into for profit are deductible only if the loss is attributable to a federally or state declared disaster.
Alimony and Separate Maintenance Payments [former 26 USC 62(a)(10), former 26 USC 71, former 26 USC 215]	According to IRS guidance, “Generally, alimony or separate maintenance payments are deductible by the payer spouse and includible in the recipient spouse's income if paid under a divorce or separation agreement executed before 2019. [The payor] can't deduct alimony or separate maintenance payments made under a divorce or separation agreement (1) executed after 2018, or (2) executed before 2019 but later modified if the modification expressly states the repeal of the deduction for alimony payments applies to the modification.” According to Department of Revenue data, in Tax Year 2021, this deduction was claimed on 8,600 federal returns filed by full-year Colorado residents for a total of about $246.8 million in deductions. Based on Colorado’s 4.5 percent income tax rate at this time, we estimate that this deduction could have reduced state tax revenue by about $11.1 million.
Qualified Tips [26 USC 63(b)(5), 26 USC 224]	The OBBBA provided for a new above-the-line deduction for certain tip income. For Tax Years 2025 through2028, Taxpayers are able to deduct qualified tips received during a tax year, not in excess of $25,000. The amount of the deduction is reduced by $100 for each $1,000 by which the taxpayer’s modified adjusted gross income exceeds $150,000. The deduction is only available to employees who work in occupations that customarily and regularly received tips prior to 2025; the Secretary of the Treasury identifies these occupations. No deduction is allowed unless the taxpayer includes their Social Security number on their tax return.

Deduction	Description
Overtime [26 USC 63(b)(6), 26 USC 225]	The OBBBA provided for new above-the-line deduction for qualified overtime compensation. For Tax Years 2025 through 2028, taxpayers are able to deduct overtime compensation received pursuant to Section 7 of the Fair Labor Standards Act, not in excess of $12,500. The amount of the deduction is reduced by $100 for each $1,000 by which the taxpayer's modified adjusted gross income exceeds $150,000. No deduction is allowed unless the taxpayer includes their Social Security number on their tax return. As noted earlier, Colorado requires any overtime excluded or deducted from a taxpayer's federal gross income be added back for purposes of determining the taxpayer's state taxable income [Section 39-22-104(3)(u), C.R.S.].
Housing Costs While Living and Working Outside the United States [26 USC 911(c)(4)(A)]	An individual whose tax home is in a foreign country and is either a citizen of the United States and a resident of a foreign country or a United States citizen or resident who spent the majority of the tax year in a foreign country may be eligible to deduct qualified housing expenses. To be eligible to be deducted, the individual's employer may not have provided the housing or covered the costs of the housing. There are several limitations on this deduction; the standard limit on housing expenses is generally 30 percent of the maximum foreign earned income exclusion, which is $132,900 per person. According to IRS guidance, for 2026, the housing amount limitation is $39,870. However, the limit also varies depending on the location of the individual's foreign source income, foreign tax home, and the number of qualifying days in the tax year.

Source: Office of the State Auditor analysis of federal laws, Internal Revenue Service taxpayer guidance documents, Internal Revenue Service data, Colorado laws, Colorado Department of Revenue taxpayer guidance documents, Colorado Department of Revenue data, and Bloomberg Law documents.

Appendix D

Itemized Deductions

This appendix provides a list of the itemized deductions that taxpayers can claim at the federal level (instead of the standard deduction). This list includes brief descriptions of the federal deductions and IRS statistics of income data showing the number of federal returns for which taxpayers used a Colorado address for filing that claimed the deductions and the total amount claimed. The data are from Tax Year 2022, which was the most recent year available. For miscellaneous itemized deductions subject to a limit, we used Tax Year 2017, which was the most recent year these deductions were available. Additionally, we indicate when Colorado has enacted legislation to deviate from the federal tax treatment of itemized deductions and the revenue impact of doing so, when data were available.

Deduction	Description
Medical and Dental Expenses [26 USC 213]	Individual taxpayers are allowed to claim as an itemized deduction eligible medical and dental care expenses incurred by themselves, their spouse, or their dependent if the expenses exceed 7.5 percent of the taxpayer’s adjusted gross income. To qualify, the expenses cannot have been compensated by insurance (or otherwise). According to IRS data for Tax Year 2022, the medical and dental care expenses deduction was claimed on 65,410 federal returns filed by Coloradans with a total amount of about $1.3 billion of deductions. Based on the State’s 4.4 percent income tax rate, we estimate that this deduction could have reduced state tax revenue by about $58.9 million in Tax Year 2022.
State and Local Income Taxes or General Sales Taxes [26 USC 164(a)(3) and (b)(5)]	Individual taxpayers are allowed to claim as an itemized deduction either state and local income taxes or state and local sales taxes paid. For tax years beginning in Calendar Year 2026, the amount is limited to $40,400 which increases by 1 percent each year through 2029, at which point the limit is lowered to $10,000. For high-income taxpayers whose modified gross income exceeds a threshold ($505,000 in Calendar Year 2026), the limitation is reduced by 30 percent of the excess (if any) of the taxpayer’s modified AGI over the threshold amount, but not below $10,000. According to IRS data for Tax Year 2022, state and local income taxes were deducted on 313,550 federal returns filed with a Colorado address, for a total of $4.9 billion in deductions. State and local sales taxes were claimed on 23,980 federal returns with a Colorado address, for a total of $43.8 million in deductions. Colorado does not fully conform to this provision of the IRC. Individuals must add back to their federal taxable income (when calculating Colorado taxable income) any state income taxes deducted as an itemized deduction on their federal return, subject to certain limitations [Section 39-22-104(3)(d), C.R.S.]. According to Department of Revenue data, in Tax Year 2021, Colorado taxpayers claimed $2.3 billion in deductions on their federal returns based on this provision and added back about $952.2 million. Based on the amount deducted on Colorado taxpayers’ federal returns, the amount added back for state income taxes, and the State’s 4.5 percent income tax rate at this time, we estimate that this deduction could have reduced state tax revenue by about $58.6 million in Tax Year 2021.

Deduction	Description
State and Local Real Estate Taxes [26 USC 164(a)(1)]	Individual taxpayers are allowed to claim as an itemized deduction state and local real property taxes. For tax years beginning in Calendar Year 2026, the amount is limited to $40,400 which increases by 1 percent each year through 2029, at which point the limit is lowered to $10,000. For high-income taxpayers whose modified gross income exceeds a threshold ($505,000 in Calendar Year 2026), the limitation is reduced by 30 percent of the excess (if any) of the taxpayer's modified AGI over the threshold amount, but not below $10,000. According to IRS data for Tax Year 2022, state and local real property taxes were deducted on 301,210 federal returns filed with a Colorado address, for a total of $1.5 billion in deductions. Based on Colorado's 4.4 percent income tax rate, we estimate that this deduction could have reduced state tax revenue by about $65 million in Tax Year 2022.
State and Local Personal Property Taxes [26 USC 164(a)(2)]	Individual taxpayers are allowed to claim as an itemized deduction state and local personal property taxes. For tax years beginning in Calendar Year 2026, the amount is limited to $40,400 which increases by 1 percent each year through 2029, at which point the limit is lowered to $10,000. For high-income taxpayers whose modified gross income exceeds a threshold ($505,000 in Calendar Year 2026), the limitation is reduced by 30 percent of the excess (if any) of the taxpayer's modified AGI over the threshold amount, but not below $10,000. According to IRS data for Tax Year 2022, state and local personal property taxes were deducted on 191,270 federal returns filed with a Colorado address, for a total of $123.0 million in deductions. Based on the State's 4.4 percent income tax rate, we estimate that this deduction could have reduced state tax revenue by about $5.4 million in Tax Year 2022.
Home Mortgage Interest, including Buyer Points [26 USC 163(h)(3)]	Individual taxpayers are allowed to claim as an itemized deduction interest and points (if the taxpayer is the buyer) the taxpayer paid on a loan secured by their main home or a second home. There may be some limitations to the deduction depending on when the mortgage was taken out. If the mortgage was taken out between October 13, 1987 and December 15, 2017, only the interest on up to $1 million of debt is deductible. If the mortgage was taken out after December 15, 2017, only the interest on $750,000 or less is deductible. Beginning January 1, 2026, taxpayers will be able to deduct the interest on up to $1 million of mortgage debt. According to IRS data for Tax Year 2022, home mortgage interest was deducted on 294,350 federal returns filed with a Colorado address, for a total of $4.0 billion in deductions. Points were deducted on 22,060 federal returns with a Colorado address for a total of $25.8 million in deductions. Based on the State's 4.4 percent income tax rate, we estimate that this provision reduced state tax revenue by about $179.3 million in Tax Year 2022.
Passenger Vehicle Loan Interest [26 USC 163(h)(4)]	For tax years 2025 through 2028, up to $10,000 of qualified passenger vehicle loan interest is deductible. For higher-income taxpayers, the allowable deduction is reduced (not below zero) by $200 for each $1,000 by which the modified adjusted gross income of the taxpayer exceeds $100,000 in the taxable year. Applicable passenger vehicles must have final assembly within the United States.

Deduction	Description
Investment Interest Paid [26 USC 163(d)]	According to IRS guidance, individual taxpayers are allowed to claim as an itemized deduction investment interest paid on money the taxpayer borrowed that is allocable to property held for investment. It does not include any interest allocable to passive activities or to securities that generate tax-exempt income. According to IRS data for Tax Year 2022, investment interest was deducted on 18,950 federal returns filed with a Colorado address, for a total of $468.8 million in deductions. Based on the State's 4.4 percent income tax rate, we estimate that this provision reduced state tax revenue by about $20.6 million in Tax Year 2022.
Charitable Contributions [26 USC 170]	Individual taxpayers are allowed to claim a deduction for contributions of eligible property to qualifying organizations, subject to limitations. In general, taxpayers may donate cash (which includes donations made by check or credit card) as well as other types of property such as stock, artwork, land or real estate, vehicles, and conservation easements. Charitable contributions must be given to the following types of organizations as a gift or for the use of the organization: (1) A state, possession of the United States, any political subdivision of a state/possession, the United States, or the District of Columbia but only if the contribution is made for exclusively public purposes. (2) A corporation, trust, community chest, fund, or foundation that is created and organized in the United States and organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals. Additionally, no part of the earnings of the organization may inure to the benefit of any private shareholder or individual and the organization cannot attempt to influence legislation and does not participate or intervene in any political campaign (either on behalf of or in opposition to) for any candidate for public office. These types of organizations, which are defined in 26 USC 501(c)(3) are classified as either public charities or private foundations. Public charities receive the majority of their support from the general public or government units and have greater interaction with the public. Common examples of public charities are museums, animal rescues, churches, schools, hospitals, and medical research organizations. According to IRS guidance, a private foundation "is typically controlled by members of a family or by a small group of individuals, and derives much of its support from a small number of sources and from investment income." (3) A post or organization of war veterans. (4) A domestic fraternal society, order, or association operating under the lodge system, but only if the contribution is used exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals. (5) A cemetery company owned and operated exclusively for the benefit of its members if the company is not operated for profit and none of its earnings inure to the benefit of a private shareholder or individual. (6) An organization described in section 501(c)(19) [26 USC 501(c)(19)] that is a federally chartered corporation. These are organizations in which at least 75 percent of the members are current or past members of the United States Armed Forces and substantially all of the other members are cadets or spouses, widows, widowers, ancestors, or lineal descendants or past or current members of the United States Armed forces or of cadets. Additionally, none of the earnings of the organization can inure to the benefit of a private shareholder or individual.

	There are limitations on the deduction amount based on what type of property is given and to what type of organization it is given. For example, donations of cash to public charities by individuals are limited to 60 percent of the taxpayer's adjusted gross income. Although Colorado generally conforms with this deduction, if a taxpayer claims a charitable contribution deduction on their federal return for the donation of a conservation easement on property located in Colorado and claims the Colorado Conservation Easement Credit pursuant to Section 39-22-522, C.R.S., they must add back the amount of the charitable contribution deduction claimed on their federal return when calculating their Colorado taxable income [Section 39-22-104(3)(g), C.R.S.]. According to IRS data for Tax Year 2022, charitable contributions were deducted on 256,140 federal returns filed with a Colorado address, for a total of $3.8 billion in deductions. Based on the State's 4.4 percent income tax rate, we estimate that this provision reduced state tax revenue by about $168.1 million in Tax Year 2022. We were not able to account for the state addback for conservation easement donations for which a state credit was claimed in our estimate because the Department of Revenue does not publish data related to this addback.
Casualty and Theft Losses [26 USC 165(c)(3)]	In general, individuals may claim an itemized deduction for a loss of property arising from fire, storm, shipwreck, or other casualty, or from theft. For each casualty or theft event, the taxpayer must reduce the loss by $100. After applying that reduction, the taxpayer may deduct the remaining losses only to the extent that their total exceeds 10 percent of adjusted gross income. For tax years beginning after 2017, casualty and theft losses of property not connected with a trade or business or transaction entered into for profit are deductible only if the loss is attributable to a federally or state declared disaster. Note that the distinction between this itemized deduction for casualty and theft losses and the above-the-line casualty and theft loss deduction allowed to be taken in calculating adjusted gross income is that this itemized deduction for a loss may be taken in excess of casualty and theft gains, which are gains that arise from insurance payments or other reimbursements received for property damaged or destroyed by casualty or theft (whereas the above-the-line deduction for losses may only be taken to the extent of casualty and theft gains). The IRS does not publish statistics related to claims of this deduction.
Wagering Losses [26 USC 165(c)(2) and (d)]	Individual taxpayers may claim as an itemized deduction a loss from wagering transactions (e.g., gambling) equal to 90 percent of the amount of such losses during a tax year and only to the extent of the gains from such transactions. This limitation applies to any deductions otherwise allowable that are incurred in carrying on any wagering transactions. For example, prior to 2018, professional gamblers could deduct certain expenses associated with gambling, such as hotels, travel, and legal and accounting fees, even when the expenses were in excess of any gains from wagering activities. The IRS does not publish statistics related to claims of this deduction.

Deduction	Description
Other Miscellaneous Itemized Deductions (non-limited)	Individual taxpayers may claim as itemized deductions several other deductions, including deductions related to impairment-related work expenses, estate tax in the case of income in respect of the decedent [26 USC 691(c)], personal property used in a short sale, computation of tax where taxpayer restores substantial amount held under claim of right [26 USC 1341], annuity payments ceasing before investment recovered [26 USC 72(b)(3)], amortizable bond premium [26 USC 171], and in connection with cooperative housing corporations [26 USC 216]. Collectively, these other itemized deductions do not have a limitation as other miscellaneous itemized deductions do (see immediately below). According to IRS data for Tax Year 2022, these other itemized deductions were deducted on 15,080 federal returns filed with a Colorado address, for a total of $535.3 million in deductions. Based on the State's 4.4 percent income tax rate, we estimate that this provision reduced state tax revenue by about $23.6 million in Tax Year 2022.
Educator Expenses [26 USC 67]	Individual taxpayers used to be able to claim several other miscellaneous deductions, subject to a limit. Specifically, these miscellaneous itemized deductions for any taxable year were only allowed to the extent that the aggregate of the deductions exceeds 2 percent of adjusted gross income. The TCJA temporarily suspended these deductions and the OBBBA made the suspension permanent. However, within this section, a new itemized deduction for educator expenses was provided for, separate from the above-the-line deduction in 26 USC 62(a)(2)(D). These expenses include those that are eligible for the above-the-line deduction, without regard for the $250 limitation, and expanded to include certain physical education/coaching expenses.

Source: Office of the State Auditor analysis of federal laws, Internal Revenue Service guidance documents, Internal Revenue Service data, and Department of Revenue data.

Appendix E

Ordinary and Necessary Business Expenses

This appendix provides a list with descriptions of the types of expenses that businesses can generally claim as ordinary and necessary business expenses under 26 USC 162. Additionally, we indicate when Colorado has enacted legislation to deviate from the federal tax treatment of business expenses and the revenue impact of doing so, when data were available. The IRS and Colorado Department of Revenue do not publish Colorado-specific data related to these provisions.

Ordinary and Necessary Business Expense	Description
Advertising Expenses	In general, expenses associated with promoting a business in order to generate more business are deductible. If the advertising is expected to increase business for over a year, the advertising expense must be capitalized. Advertising includes traditional advertising (e.g., ads in magazines, billboards, or social media, television commercials), business gifts or samples given to prospective customers, and event or sports team sponsorship.
Charitable Contributions (as Business Expenses)	Certain charitable contributions may be deductible as business expenses rather than charitable contributions. In order to qualify as a business expense deductible under 26 USC 162, the charitable contribution must be made to a charitable organization (as defined in 26 USC 170(c)) and the contribution must have a direct relationship to the business and the contribution must be made with a reasonable expectation of financial return. Charitable contributions made not as a business expense are discussed in Appendix F.
Commuting Costs	This includes traveling between jobs or clients but not commuting between the taxpayer's residence and work location.
Compensation	Businesses may deduct a reasonable allowance for salaries or other compensation for personal services actually rendered. Although compensation (which includes wages, bonuses, and severance pay) is generally an allowable business expense deduction, the compensation must be reasonable. Publicly held corporations and controlled group members generally cannot deduct excessive compensation (i.e., more than $1 million) paid to certain employees [26 USC 162(m)]. Colorado statutes [Section 39-22-304(2)(h) and 529, C.R.S.] require that companies that deducted on their federal returns expenses related wages or remuneration paid to unauthorized aliens in excess of $600 pursuant to 26 USC 162(a)(1) to add back the amount deducted on their federal return, subject to a few exceptions. First, if the business is exempt from compliance with federal employment verification procedures under federal law that makes the employment of unauthorized aliens unlawful, then it does not have to add the deduction back. It also does not have to add back the deduction if the individual was hired prior to December 31, 2006, the individual is not directly compensated or employed by the taxpayer, or the individual holds and presents a valid license or identification card issued by the Department of Revenue.

Ordinary and Necessary Business Expense	Description
Conventions and Seminars	Businesses can deduct the cost of sending employees to business conventions and seminars if it is directly related to the business.
Costs to Protect the Business	Businesses can deduct costs to protect the business. Examples of these costs include some litigation expenses like patent infringement, and costs of investigating employees to minimize theft and embezzlement.
Educational Expenses for Employees	Educational expenses employers incur to provide education and training to employees are deductible. To qualify for a deduction, the expense must maintain or improve the employee's skills related to the position in the business or the education the employee is receiving is to meet a legal or regulatory requirement necessary for the employee to stay in their position. However, the expenses are not deductible if either the education is required for the employee to meet the minimum education requirements of the position in the business or if the education is being pursued by the employee so they can work in a new trade or business.
Employee Business Expenses	An employer can deduct expenses that an employee incurred and that the employer reimbursed as business expenses as long as the expenses are ordinary and necessary business expenses related to the trade or business.
Expenses Related to Vehicles Used in the Business	Expenses related to vehicles used by a business can be deducted. Examples of these expenses include gas, oil, and insurance or the standard mileage rates. The vehicle itself typically must be capitalized and depreciated.
Government Taxes and Fees	Taxes and fees imposed on businesses by governments are deductible. Note that some taxes are generally deductible under 26 USC 164 even if they are not connected to a trade or business, such as foreign, state, and local income taxes; foreign, state, or local real property taxes; and state and local personal property taxes. Additional taxes and fees imposed by governments may be deducted under 26 USC 162 as ordinary and necessary business expenses, including automobile inspection or emissions testing fees if the vehicles are used in the business, license fees, utility charges, sales taxes, excise taxes, severance taxes, and tolls paid while using a vehicle for business reasons. Colorado does not fully conform to this provision of the IRC. Corporations are required to add back any income, war profits, or excess profits paid to a foreign country or possession of the United States and Colorado income taxes deducted on their federal return per Section 39-22-304(2)(a) and (d), C.R.S. According to Department of Revenue data, in Tax Year 2021, Colorado income taxes were added back on 7,570 corporate returns with a total amount of about $1.5 billion added back.
Insurance	Various types of insurance premiums may be deductible by a business, including, for example, insurance to cover theft, flood, merchandise and inventory, fire, public or employer liability, malpractice, automobile, workers' compensation, unemployment, disability, and employees' group health. Note that health insurance premiums paid by the corporation on behalf of its employees are deductible only if, when viewed together with all of the employee's other compensation, the premiums do not amount to unreasonable compensation.

Ordinary and Necessary Business Expense	Description
Interest Expense	Interest paid on loans made for business purposes is generally deductible. However, interest on loans used to purchase property must be capitalized.
Meal Expenses	Meal expenses are deductible only if they are ordinary and necessary trade expenses, and only 50 percent of the business meal expenses are deductible. In general, business entertainment expenses and (starting in 2026) employer-provided meals are not deductible, although the OBBBA provided limited exceptions for certain industries, including fishing vessels and restaurants [26 USC 274]. For tax years 2024 through 2030, Colorado does not conform to this provision of the IRC. During those tax years, a corporation that claims a federal deduction for business meals must add back the amount deducted when calculating their Colorado taxable income [Section 39-22-304(2)(k)(I), C.R.S.].
Membership Dues	Membership dues are deductible business expenses only if related to the business, for example, membership in a trade association or chamber of commerce.
Moving Expenses	Moving expenses related to moving the business's equipment, machinery, office contents, and personnel are deductible.
Phone Expenses	The cost of making calls for business purposes is deductible, such as when businesses provide cell phones to their employees for business purposes.
Professional Services	Fees paid for professional services, such as accounting, actuarial services, appraisals, investment and business advice, and legal services, are generally deductible.
Repairs	Expenses associated with repairing property used in the business is generally deductible as long as the work does not improve the property in a way that makes its value appreciate or extends its life significantly; in those cases, the repair costs must be capitalized.
Safety Devices	Expenses related to maintaining and operating safety devices are deductible. The safety devices themselves may need to be capitalized, depending on their expected useful life.
Supplies	Supplies and materials that are consumed during the year are deductible.
Transportation	The cost of moving people, goods, or equipment between business locations for a business reason is deductible.

Source: Office of the State Auditor analysis of federal laws, Colorado laws, Bloomberg Law documents, and Colorado Department of Revenue data.

Appendix F

Various Business Expenses Deductions

This appendix provides a list with descriptions of the types of expenses that businesses can generally deduct under various sections of the IRC. Additionally, we indicate when Colorado has enacted legislation to deviate from the federal tax treatment of business expenses and the revenue impact of doing so, when data were available.

Deduction	Description
Amortization of Certain Intangibles [26 USC 197]	Allows businesses to claim a deduction for amortization, which is the process of spreading the cost of intangibles over their useful life, of certain intangibles, including goodwill; going concern value; workforce in place including its composition and terms and conditions of its employment; business books and records, operating systems, or any other information base (including lists or other information with respect to current or prospective customers); patents, copyrights, formulas, processes, designs, patterns, knowhow, format, or other similar items; licenses, permits, or other rights granted by a government unit; covenants not to compete entered into in connection with an acquisition of an interest in a trade or business; franchise, trademark, or trade name; customer-based intangibles (e.g., composition of market, market share); and supplier-based intangibles (i.e., any value resulting from future acquisition of goods or services pursuant to relationships in the ordinary source of business with suppliers to be used or sold by the taxpayer). Certain types of intangibles are not allowed to be amortized under 26 USC 197, including financial interests in a corporation, partnership, trust, or estate; financial interests under an existing futures contract, foreign currency contract, or other similar financial contract; land; and certain types of computer software. The amortization period is 15 years. The annual deductible amount is determined by dividing the adjusted basis of the asset by 15. For example, if the adjusted basis of the intangible asset is $15,000, the taxpayer could claim $1,000 per year for 15 years.
Antitrust, Infringement, and Contractual Losses [26 USC 186]	If the taxpayer includes in gross income a compensatory amount that is received or accrued during the year for a compensable injury, they may deduct the lesser of the compensatory amount or the amount of the unrecovered losses sustained as a result of the injury. According to United States Treasury Regulations [26 CFR 1.186-1(b)(1)], there are three types of compensable injuries: (1) an injury sustained as a result of an infringement of a patent issued by the United States, (2) an injury sustained as a result of a breach of contract or a breach of fiduciary duty or relationship, and (3) an injury sustained in business or to property by reason of any conduct forbidden in the antitrust laws for which a civil action may be brought under the Clayton Act.
Architectural and Transportation Barrier Removal Expenditures [26 USC 190]	A taxpayer may elect to deduct (rather than capitalize) expenditures for removing architectural and transportation barriers to make the facility used in connection with their trade or business more accessible to and usable by handicapped and elderly individuals. The deduction is limited to $15,000. Any remaining expenditures over $15,000 must be capitalized.

Deduction	Description
Asset Expensing [26 USC 179]	A taxpayer may elect to deduct (rather than capitalize and depreciate) the cost of certain property, up to a certain amount in the year in which the property is placed into service. The aggregate cost that can be deducted is limited to $2.5 million, but that limit is reduced if the cost of the property exceeds $4 million. Additionally, only up to $25,000 may be deducted for the cost of a sport utility vehicle. These amounts are adjusted annually for inflation. Property eligible to be deducted under 26 USC 179 includes tangible property normally required to be depreciated, certain computer software normally required to be depreciated, and certain real property (i.e., improvements to interiors of nonresidential real property, roofs, HVAC property, fire protection and alarm systems, security systems), which is acquired for use in the active conduct or a trade or business. Deductions claimed under 26 USC 179 cannot create or increase a business's net operating loss.
Bad Debts [26 USC 166]	Corporations may deduct bad debts that are bona fide legally enforceable debts that have become worthless.
Charitable Contributions [26 USC 170]	Corporations may deduct charitable contributions made to qualifying organizations (i.e., governmental units, certain charitable organizations recognized under 26 USC 501(c)(3), certain veterans' organizations, and nonprofit cemetery companies). The deduction is only allowed to the extent that aggregate contributions exceed 1 percent of the taxpayer's taxable income for the tax year. A corporation may only deduct an amount up to 10 percent of its federal taxable income; qualifying donation amounts that exceed 10 percent of the corporation's federal taxable income can be carried forward for 5 years. If a taxpayer claims a charitable contribution deduction on their federal return for the donation of a conservation easement on property located in Colorado and claims the Colorado Conservation Easement Credit pursuant to Section 39-22-522, C.R.S., they must add back the amount of the charitable contribution deduction claimed on their federal return when calculating their Colorado taxable income [Section 39-22-304(2)(f), C.R.S.].
Contributions to Employee Plans [26 USC 404]	Subject to numerous rules and limitations, employers may deduct contributions to stock bonus, pension, profit-sharing, or annuity plans and payments or accruals of deferred compensation.
Depreciation [26 USC 167, 26 USC 168]	Taxpayers are allowed to claim a deduction for depreciation, which is reasonable allowance for the exhaustion, wear, and tear (including a reasonable allowance for obsolescence) of property used in a trade or business or property held for the production of income. The IRC [26 USC 168] generally provides the method and recovery period over which different classes of property must be depreciated. Most types of tangible property (real and personal) are depreciated over 3, 5, 7, 10, 15, 20, 25, 27.5, 39, or 50 years. For businesses that cannot use full asset expensing under 26 USC 179, the OBBBA created a special bonus depreciation provision in 26 USC 168(k) that allowed businesses to fully depreciate certain assets in the year in which they were placed in service.

Deduction	Description
Energy Efficient Commercial Building Property [26 USC 179D]	Taxpayers may elect to deduct the costs of installing energy-efficient commercial building property rather than capitalizing and depreciating it. The deductible amount is limited based on a dollar amount set in statute (between $0.50 and $1.00 depending on reduction in energy and power costs) and the square footage of the building. If the property satisfies certain prevailing wage requirements and apprenticeship requirements, then the deduction amount can be increased. The OBBBA eliminated this deduction for property beginning construction after June 30, 2026.
Losses Incurred by the Business [26 USC 165]	In general, businesses are allowed to deduct "any loss sustained during the taxable year and not compensated for by insurance or otherwise."
Start-up Expenditures [26 USC 195]	Start-up expenditures are any amounts paid or incurred in connection with (1) investigating the creation or acquisition of an active trade or business, (2) creating an active trade or business, or (3) any activity engaged in for profit and for the production of income before the day on which the active trade or business begins, in anticipation of such activity becoming an active trade or business, and which, if paid or incurred in connection with the operation of an existing active trade or business would be allowable as a deduction for the taxable year in which paid or incurred. Start-up expenditures do not include interest on indebtedness normally deductible under 26 USC 163(a), taxes normally deductible under 26 USC 164, or amortization of research and experimental expenditures normally amortized and deducted under 26 USC 174. Some examples of start-up expenditures include surveys and market/feasibility studies; advertising done in advance of the business opening; compensation paid to employees that join the company before it opens; and training employees before the company opens. Start-up expenses are generally not deductible; however, 26 USC 195 allows taxpayers to elect to deduct start-up expenditures, up to a certain amount. The taxpayer may deduct up to $5,000 of start-up expenditures, but the $5,000 is reduced by the amount by which the start-up expenditures exceed $50,000. Any remaining start-up expenditures are allowed as a deduction ratably over the 180-month period beginning in the month that the active trade or business begins.
Unused Business Credits [26 USC 196]	Businesses can deduct parts of certain business credits that were not able to be fully claimed because the carryforward period for the credit expired or the taxpayer ceased to exist. This deduction applies to the following credits: the investment credit (limited to 50 percent of the unused credit) [26 USC 46], the work opportunity credit [26 USC 51(a)], the alcohol fuels credit [26 USC 40(a)], the research credit [26 USC 41(a)], the enhanced oil recovery credit [26 USC 43(a)], the empowerment zone employment credit [26 USC 1396(a)], the Indian employment credit [26 USC 45A(a)], the employer Social Security credit [26 USC 45B(a)], the new markets tax credit [26 USC 45D(a)], the small employer pension plan startup cost credit [26 USC 45E(a)], the biodiesel fuels credit [26 USC 40A(a)], the low sulfur diesel fuel production credit [26 USC 45H(a)], the new energy efficient home credit [26 USC 45L(a)], and the small employer health insurance credit [26 USC 45R(a)].

Source: Office of the State Auditor analysis of federal laws and regulations, Internal Revenue Service guidance, and Colorado laws.

Appendix G

Corporate "Special Deductions"

Corporations are allowed to claim additional "special deductions" when calculating federal taxable income [26 USC 241]. This appendix provides a list with descriptions of the special deductions allowed. Additionally, we indicate when Colorado has enacted legislation to deviate from the federal allowance of special deductions.

Special Deduction	Description
Dividends Received by Corporations [26 USC 243]	Domestic corporations are allowed to claim a deduction for a portion of the dividends received from domestic corporations for which they have an ownership interest. The percentage that they are allowed to claim depends on the ownership percentage in the company. Corporate shareholders that own less than 20 percent of the corporation from which they are receiving dividends are allowed to claim a deduction for 50 percent of the dividends received. If the company owns 20 percent or more of the stock of the distributing company, the company receiving dividends can deduct 65 percent of the dividends received. If a company is a part of the same affiliated group for federal tax purposes, it may generally deduct all of the dividends received. According to Bloomberg Law, the purpose of the dividends received deduction is "to impose a single corporate income tax on the same domestic income. Without the DRD [dividends received deduction], domestic corporate income could be subjected to double taxation; first when earned, and then when distributed to corporate shareholders…without the relief of the DRD, the same earnings could be subject to more than two levels of taxation as distributions are made to corporate shareholders and then to individual shareholders."
Dividends Received from Certain Foreign Corporations [26 USC 245]	Domestic corporations that own at least 10 percent of a foreign corporation are allowed to claim a deduction for a portion of the dividends they receive from the foreign corporation. The deductible dividends received from the foreign corporation are generally the US-source portion of a dividend that is attributable to income of the corporation that is connected with a U.S. business or dividends received by the foreign corporation from a U.S. subsidiary. The percentage of the deduction is typically determined by the same stock ownership percentages for the dividends received deduction in 26 USC 243. The deduction is allowed for all of the dividends distributed from wholly owned foreign subsidiaries in certain circumstances.
Dividends Received by Domestic Corporations from Certain 10-percent Owned Foreign Corporations [26 USC 245A]	Domestic corporations are allowed to claim a deduction for the foreign-source portion of dividends received from certain foreign corporations. The amount of foreign source dividend that may be deducted is calculated by multiplying the dividend received by the U.S. corporation by a fraction, which is calculated as the undistributed foreign earnings of the corporation divided by the total undistributed earnings.

Special Deduction	Description
Organizational Expenditures [26 USC 248]	An organizational expenditure is defined in federal law [26 USC 248(b)] as "any expenditure which – (1) is incident to the creation of the corporation; (2) is chargeable to capital account; and (3) is of a character which, if expended incident to the creation of a corporation having a limited life, would be amortizable over such life." Treasury regulation [26 CFR 1.248-1(b)(2)] provides examples of organizational expenditures that qualify for this election, which include "legal services incident to the organization of the corporation, such as drafting the corporate charter, by-laws, minutes of organizational meetings, terms of original stock certificates, and the like; necessary accounting services; expenses of temporary directors and of organizational meetings of directors or stockholders; and fees paid to the State of incorporation." A corporation may elect to deduct organizational expenditures, subject to a limit, in the taxable year in which it begins business. If the corporation makes the election, it may deduct up to $5,000 of organizational expenditures, but the $5,000 is reduced by the expenditure amount that exceeds $50,000. The remainder of the organizational expenditures is deducted ratably over the 180-month period beginning with the month in which the corporation begins business.

Special Deduction	Description
Foreign-derived Deduction Eligible Income and Net CFC Tested Income [26 USC 250]	Prior to 2017, only certain types of foreign income were taxed annually (e.g., royalties, interest, dividends) but other types of foreign income were only taxed when they were repatriated to the U.S. Federal taxation of multinational entities (MNEs) changed notably under the TCJA, which expanded the attribution of income from controlled foreign corporations (CFCs) to U.S. shareholders under subpart F to address income shifting, along with provisions that created certain targeted effective tax rates on the exports of MNEs. Overall, these policies are intended to disincentivize companies from locating their intangible assets in foreign jurisdictions. First, "Global Intangible Low Taxed Income" (GILTI) was established by including the parent's share of the CFCs aggregate income in the tax year (i.e. net CFC tested income) in the shareholder or parent's income to the extent it exceeds a 10 percent return on the CFC's tangible assets (i.e., the qualified business asset investment or QBAI reduction), excluding net tested losses. To achieve a 13.125 percent effective corporate tax rate on GILTI, a 50 percent special deduction was allowed for corporate shareholders, along with a foreign tax credit (FTC) equal to 80 percent of tax paid. To achieve the same 13.125 percent effective federal corporate tax rate on income from export activities of domestic entities, Foreign-Derived Intangible Income (FDII) was computed and reduced by the same QBAI amount as GILTI and a 37.5 percent special deduction for this income was allowed. The OBBBA replaced the international taxing regimes established by the TCJA. Specifically, GILTI was replaced with net CFC tested income (NCTI) and FDII was replaced with foreign-derived deduction eligible income (FDDEI). The new law changed the net CFC tested income calculation by reducing certain expenses allocable to NCTI like interest and research expenses and re-allocating them instead to U.S. sourced income, as well as eliminating the QBAI reduction from GILTI (now NCTI) and FDII (now FDDEI). According to the Multistate Tax Commission, this was done to reduce the incentive for U.S. corporations to move tangible assets abroad in order to increase the QBAI amount. Additionally, the special deduction for NCTI was reduced from 50 percent to 40 percent and the allowable FTC was increased from 80 percent to 90 percent to achieve a targeted effective corporate tax rate of 14 percent. The special deduction for FDDEI was reduced from 37.5 percent to 33.34 percent to achieve the same targeted effective corporate tax rate of 14 percent. Colorado statute [Section 39-22-304(3)(j), C.R.S.] allows corporations to deduct amounts treated as dividends under 26 USC 78 when calculating their Colorado taxable income. However, the deduction is not allowed for amounts treated as a dividend under 26 USC 78 that are attributable to GILTI/NCTI and deducted under 26 USC 250(a)(1)(B)(ii).

Source: Office of the State Auditor analysis of federal laws and regulations, Internal Revenue Service guidance, Department of Revenue guidance, and Bloomberg Law documents.

Appendix H

Colorado Tax Credits Calculated Based on Similar Federal Tax Credits

This appendix provides descriptions of three Colorado income tax credits, which are all available to individuals, that are calculated based on a percentage of a similar federal credit.

The Child and Dependent Care Expenses Income Tax Credit [Section 39-22-119, C.R.S.] allows Colorado resident individual taxpayers who claim a credit for child and dependent care expenses on their federal tax return, as allowed under 26 USC 21, to claim a refundable Colorado income tax credit equal to 70 percent of the federal credit. The federal credit is not refundable. The Colorado credit is limited to taxpayers with $60,000 or less in federal adjusted gross income. Beginning in Tax Year 2026, the Colorado credit amount is calculated as if the federal credit were fully refundable, which will make it available to taxpayers with lower incomes who lack sufficient tax liability to qualify for the federal credit due to it not being refundable. Beginning in Tax Year 2027, the adjusted gross income cap to qualify for the credit will be adjusted for inflation.

The Department of Revenue combines data for this credit with another similar child and dependent care expenses income tax credit that is specifically for taxpayers with lower incomes who are not eligible for the federal credit due to lacking sufficient tax liability. That credit expired at the end of 2025 and the credit in Section 39-22-119, C.R.S. has been amended so that taxpayers with lower incomes can claim it instead. According to Department of Revenue data, in Tax Year 2023, which was the most recent year of data available, the combined revenue impact of both child and dependent care expense tax credits was about $5.2 million, with the average credit being $291. It was claimed by about 17,940 taxpayers. Our office published an **evaluation** of this credit in 2023; note that the credit was amended in the 2024 Legislative Session and changes to the credit are not reflected in our 2023 evaluation of it.

The Colorado Earned Income Tax Credit (EITC) [Section 39-22-123.5, C.R.S.] is a refundable income tax credit for working taxpayers whose earned income is below a certain amount and who claim the federal earned income tax credit. In general, in order to be eligible for the Colorado EITC, the taxpayer must have been eligible for the federal EITC. The Colorado EITC amount is a percentage of the taxpayer's federal EITC, and the percentage varies by year. In Tax Years 2024 and 2025, the Colorado EITC is 50 percent of the federal EITC, and in 2026 and later the Colorado EITC is 25 percent of the federal EITC. The percent in a given tax year may be increased based on an adjustment factor, which is calculated as the forecasted compound annual growth of state revenue subject to TABOR. The federal EITC amount varies depending on filing status (e.g., single, married filing jointly), number of children, and adjusted gross income. For example, in 2025, the maximum amount of adjusted gross income a single taxpayer with one child could have had to qualify was $50,434 and the maximum EITC they could claim was $4,328.

There are a couple of exceptions for when a Colorado taxpayer may claim the Colorado EITC when they were not eligible for the federal EITC. First, according to Department of Revenue guidance, "the Colorado EITC…is allowed to resident individuals based on the federal EITC they would have been allowed, but were not allowed solely because the resident individual, their spouse, or one or more of their dependents did not have a social security number (SSN) that is valid for employment." Second, resident individuals who are under 25 years of age and do not have a qualifying child and do not qualify for the federal EITC may be eligible if they have a work-eligible social security number and either 24 years of age and a specified student, between 19 and 24 and not a specified student, or between 18 and 24 and are a qualified former foster youth or qualified homeless youth.

According to Department of Revenue data, in Tax Year 2023, which was the most recent year of data available, about 311,000 Colorado taxpayers that claimed the federal EITC claimed about $356.5 million in Colorado EITCs, with an average credit of $1,145. About an additional 32,000 Colorado taxpayers claimed about $23.1 million in Colorado EITCs under one of the two exceptions above, with an average credit of $711. Our office published an **evaluation** of this credit in 2022; note that the General Assembly amended the credit in the 2023 through 2026 Legislative Sessions, and changes made to the credit are not reflected in our 2022 evaluation of it.

Colorado Minimum Tax Credit [Section 39-22-105(3), C.R.S.] Some individual taxpayers may need to calculate and pay federal alternative minimum tax (AMT). To determine whether they owe federal AMT, taxpayers must generally calculate their federal AMT income by first adding exclusion and deferral items to their regular federal taxable income. Exclusion items include things that permanently reduce their federal taxable income like business operating expenses and interest. Deferral items are things that generally do not cause a permanent difference in taxable income because there is a corresponding increase in taxable income in later years, such as accelerated depreciation. After adding exclusion and deferral items to their regular federal taxable income, taxpayers then subtract a federal AMT exemption amount. In Tax Year 2026, the exemption amount was $90,100 for single filers and $140,200 for joint filers (the exemption amount is phased out for taxpayers with over a certain amount of income). They then multiply their federal AMT income by a rate, set between 26 and 28 percent based on their income level and filing status, to determine their federal AMT. Federal AMT is only paid to the extent that it exceeds their regular federal tax liability. For example, if a taxpayer's federal AMT is $20,000 and their regular federal income tax liability is $18,000, they would owe $2,000 in federal AMT as well as $18,000 in regular federal income tax. According to Department of Revenue guidance, "Colorado law establishes an alternative minimum tax (AMT) for individuals. Colorado AMT is based largely on federal alternative minimum taxable income, making it likely that a taxpayer who owes federal AMT will also owe Colorado AMT. The Colorado AMT is in addition to the normal Colorado income tax a taxpayer owes and is equal to the amount by which the tentative minimum tax exceeds the normal tax."

Federal law allows individuals who were liable for federal AMT in the prior tax year, but are no longer liable for it in the current tax year, to claim a federal AMT credit against their federal income tax. The credit allows taxpayers to recoup the additional taxes they paid due to deferral items they claimed in the prior year that caused them to owe AMT. For example, if a taxpayer was subject to the federal AMT in the prior year solely because they claimed a deferral item, such as the accelerated depreciation deduction, but they no longer owe federal AMT in the current year, they could claim the federal AMT credit. The taxpayer would also then qualify for the Colorado Minimum Tax Credit against their Colorado income tax, which is calculated as 12 percent of the federal AMT credit amount. According to Department of Revenue data, in Tax Year 2023, which was the most recent year of data available, the revenue impact of the Colorado Minimum Tax Credit was about $5.0 million, with the average credit being $1,286. It was claimed by about 3,900 taxpayers. Our office published an **evaluation** of this credit in 2021. It has not been changed since our evaluation of it.

Appendix I

Organizations Exempt from Federal Income Tax

This appendix provides a list of the types of organizations that are exempt from federal income tax under federal law and the IRC section under which they receive their tax-exempt status.

- A trust created or organized in the United States that forms a part of a stock bonus, pension, or profit-sharing plan of an employer for the exclusive benefit of its employees or their beneficiaries that is described in 26 USC 401(a) [26 USC 501(a)]. According to Bloomberg Law, these types of organizations "comprise a substantial segment of exempt organizations."
- Corporations Organized Under an Act of Congress [26 USC 501(c)(1)].
- Title Holding Corporations [26 USC 501(c)(2)].
- Charitable, Religious, Educational, Scientific, etc. Organizations [26 USC 501(c)(3)]. Only organizations described in this section (except for testing for public safety organizations) are eligible to receive tax-deductible contributions [26 USC 170]. As such, there are additional qualifications for these types of organizations to receive tax-exempt status. Organizations exempt under 26 USC 501(c)(3) must be organized and exclusively for exempt purposes set forth in 26 USC 501(c)(3), including "religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals…" Additionally, no part of the net earnings of the organization may inure to the benefit of a private individual. There are also substantial limitations of the amount of political activities that organizations exempt under 26 USC 501(c)(3) are allowed to engage in: no substantial part of the activities of the organization may involve carrying on propaganda or otherwise attempt to influence legislation (with some exceptions provided in statute), and the organization cannot participate in or intervene in political campaigns on behalf of or in opposition to any candidates for public office.
- Civic Leagues and Social Welfare Organizations [26 USC 501(c)(4)].
- Labor, Agricultural, and Horticultural Organizations [26 USC 501(c)(5)].
- Business Leagues, etc. [26 USC 501(c)(6)].
- Social and Recreation Clubs [26 USC 501(c)(7)].
- Fraternal Beneficiary and Domestic Fraternal Societies and Associations [26 USC 501(c)(8) and (c)(10)].
- Voluntary Employees' Beneficiary Associations [26 USC 501(c)(9)].
- Teachers' Retirement Fund Associations [26 USC 501(c)(11)].
- Benevolent Life Insurance Associations, Mutual Ditch or Irrigation Companies, Mutual or Cooperative Telephone Companies, etc. [26 USC 501(c)(12)].

- Cemetery Companies [26 USC 501(c)(13)].
- State-Chartered Credit Unions, Mutual Reserve Funds [26 USC 501(c)(14)].
- Insurance Companies or Associations Other Than Life [26 USC 501(c)(15)].
- Cooperative Organizations to Finance Crop Operations [26 USC 501(c)(16)].
- Supplemental Unemployment Benefit Trusts [26 USC 501(c)(17)].
- Employee Funded Pension Trusts (created before June 25, 1959) [26 USC 501(c)(18)].
- Organizations of Past or Present Members of the Armed Forces [26 USC 501(c)(19) and (c)(23)].
- Black Lung Benefit Trusts [26 USC 501(c)(21)].
- Withdrawal Liability Payment Funds [26 USC 501(c)(22)].
- Trusts described in section 4049 of the Employer Retirement Income Security Act [26 USC 501(c)(24)].
- Title Holding Corporations or Trusts [26 USC 501(c)(25)].
- State-Sponsored Organizations Providing Health Coverage for High-Risk Individuals [26 USC 501(c)(26)].
- State-Sponsored Workmen's Compensation and Insurance and Reinsurance Organizations [26 USC 501(c)(27)].
- National Railroad Retirement Investment Trust [26 USC 501(c)(28)].
- Qualified Nonprofit Health Insurance Issuers [26 USC 501(c)(29)].
- Religious and Apostolic Associations [26 USC 501(d)].
- Cooperative Hospital Service Organizations [26 USC 501(e)].
- Cooperative Service Organizations of Operating Educational Organizations [26 USC 501(f)].
- Amateur Sports Organizations [26 USC 501(j)].
- Child Care Organizations [26 USC 501(k)].
- Charitable Risk Pools [26 USC 501(n)].
- Political Organizations [26 USC 527]. According to IRS guidance, “A political organization subject to section 527 is a party, committee, association, fund, or other organization (whether or not incorporated) organized and operated primarily for the purpose of directly or indirectly accepting contributions or making expenditures, or both, for an exempt function. ‘Exempt functions of a political organization include “influencing or attempting to influence the selection, nomination, election or appointment of an individual to a federal, state, or local public office or office in a political organization.’ A political organization must be organized and operated for the primary purpose of carrying on exempt function activities. A political organization’s primary activities must be exempt function activities. A political organization may engage in activities that are not exempt function activities, but these may not be its primary activities.”