Amendment ?: Changes to the State Income Tax Rate

Amendment ? proposes amending the <u>Colorado Constitution and Colorado statutes</u> to:

- replace the state's current flat income tax rate with a graduated tax for individual taxpayers by lowering the tax rate on all taxable income up to $250,000, and raising the tax rates on the portion of taxable income above this amount; and
- increase state income tax revenue, with the requirement that at least half of the new revenue be spent on pre-primary through twelfth grade (P-12) public education.

What Your Vote Means

YES A "yes" vote on Amendment ? changes the state individual income tax from a rate of 4.63 percent for all taxable income to rates ranging from 4.58 percent to 8.90 percent for different levels of taxable income, and requires that at least half of the new revenue be spent on P-12 education.

NO A "no" vote on Amendment ? keeps the state's individual income tax rate at 4.63 percent for all taxable income.

Summary and Analysis of Amendment ?

This analysis provides background information on the current state income tax and explains how state income taxes would change under the measure. It also describes the measure's spending and oversight requirements.

Background on Colorado's Income Tax

State income tax revenue is the largest source of funding for state government operations. Until 1987, Colorado used a graduated income tax, with different tax rates that applied to different levels of income. The Colorado Constitution was amended in 1992 to require that all taxable income be taxed at the same rate.

Since 2000, income taxpayers, including individuals and corporations, have paid a state income tax rate of 4.63 percent. For individuals, taxable income includes money earned from wages; investments; ownership of a sole proprietorship, limited liability corporation, or similar business; and certain retirement benefits, after accounting for federal and state income tax additions and deductions.

How does Amendment ? change tax rates in Colorado?

Amendment ? changes the Colorado Constitution to allow income to be taxed at different rates and replaces the current flat income tax rate with a graduated income tax. A graduated income tax applies different tax rates to different levels of income, with each rate applying only to taxable income at that level. The new rates established by the measure are:

- 4.58 percent for the portion of taxable income up to $250,000;
- 7.00 percent for the portion of taxable income over $250,000, up to $500,000;
- 7.75 percent for the portion of taxable income over $500,000, up to $1,000,000; and
- 8.90 percent for the portion of taxable income over $1,000,000.

These rates apply to the taxable income of individuals, including single and joint filers; estates; and trusts beginning in 2021. Annually beginning in 2022, the income tax levels at which the different tax rates apply will be adjusted based on changes in Colorado personal income, which is an economic measure of income earned by all households in the state.

The tax rate for corporate income is not affected and will remain at 4.63 percent.

How does the measure affect taxpayers at different income levels?

Table 1 shows how the measure would change 2021 income taxes for taxpayers with different taxable incomes. For example, a taxpayer with taxable income of $300,000 would pay a tax of 4.58 percent on the first $250,000 of their income and 7.00 percent on the remaining $50,000.

Table 1
Income Taxes Under Current Law and Amendment ?, Tax Year 2021

Taxable Income	Tax Owed at Current Rate of 4.63%	Tax Owed Under Amendment ?	Change in Tax Owed Under Amendment ?
$25,000	$1,158	$1,145	-$13
$50,000	$2,315	$2,290	-$25
$75,000	$3,473	$3,435	-$38
$150,000	$6,945	$6,870	-$75
$250,000	$11,575	$11,450	-$125
$300,000	$13,890	$14,950	+$1,060
$500,000	$23,150	$28,950	+$5,800
$1,000,000	$46,300	$67,700	+$21,400
$1,500,000	$69,450	$112,200	+$42,750

Table 2 shows the share of Colorado taxpayers whose maximum taxable income was in each tax bracket in 2018, as well as the share of total state taxable income in each tax bracket. For example, 0.3 percent of taxpayers had taxable income over $1.0 million, and the income these taxpayers earned over $1.0 million was 10.3 percent of all taxable income earned in the state. More than one of the tax rates below could apply to an individual's income, as each rate applies only to the portion of income earned in that bracket.

Table 2
Distribution of Colorado Taxpayers and Taxable Income, 2018

Taxable Income is Between…	Tax Rate Under Measure*	Share of Taxpayers with Maximum Income in Each Bracket	Share of Total Taxable Income in Each Bracket
$0 and $250,000	4.58%	97.1%	78.1%
$250,001 and $500,000	7.00%	2.0%	7.1%
$500,001 and $1,000,000	7.75%	0.6%	4.5%
$1,000,001 and up	8.90%	0.3%	10.3%

**The measure applies these rates only to the portion of income that falls into each tax bracket.*

How will the new revenue be spent?

Under the measure, the state is estimated to collect new tax revenue of up to $2.0 billion in state budget year 2021-22. This estimate was required to be prepared in February 2020 for inclusion in the ballot question, prior to the COVID-19 pandemic. Because economic conditions have worsened in the months following preparation of the estimate, the actual amount by which revenue will increase is expected to be less than estimated. The amount collected will depend on the speed of the economic recovery and its effects on taxpayers of different income levels. If approved, Amendment ? would allow the state to retain and spend the new revenue generated by the graduated income tax in the measure, up to $2.0 billion, in state budget year 2021-22.

The measure allows the state to keep and spend the new revenue and exempts it from the state's constitutional revenue limit. At least half of the new revenue must be spent to add to existing pre-primary through twelfth grade (P-12) public education funding.

The measure requires that the portion of new revenue spent on education be used to recruit, retain, and pay teachers and student service providers, and to fund categorical programs. Categorical programs include special education, English language learning, gifted and talented programs, career and technical education programs, and transportation.

Any remaining amount above what is spent on education must be used "to address the impacts of a growing population and a changing economy." The state legislature will determine how to spend these funds. At least 90 percent of the revenue must be spent on services for Coloradans and not on administrative costs.

Oversight Provisions

The measure instructs the state legislature to create a citizen's oversight committee to monitor how the revenue is spent. It also requires nonpartisan legislative staff to publicly report each year on how much revenue is generated and how the funds are spent.

In addition, the measure requires the creation of a Fair Tax Review Commission by July 1, 2029. The commission will report to the Governor by 2031 on the new income tax structure's effects on state revenue, funding of public services, distribution of income taxes among taxpayers, and the state's business climate, and recommend potential changes to the tax structure. This 25-member commission will consist of representatives from the legislative and executive branches of state government; local governments; higher education; the legal, tax, and finance professions; small and large businesses; a nonprofit organization; and the general public.

> For information on those issue committees that support or oppose the measures on the ballot at the November 3, 2020, election, go to the Colorado Secretary of State's elections center web site hyperlink for ballot and initiative information:
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> *http://www.sos.state.co.us/pubs/elections/Initiatives/InitiativesHome.html*

Arguments For Amendment ?

1) Amendment ? provides critically needed funding for Colorado's schools. Colorado spends less on education per student than most other states, with low teacher pay limiting school districts' ability to recruit and retain highly qualified teachers. State funding for P-12 education never fully recovered from cuts made during the Great Recession, and, because of the COVID-19 pandemic, funding has been reduced by an additional 10 percent this year. It is imperative that the state adequately and equitably fund a high quality education system for all of Colorado's students.

2) The measure corrects a tax system that imposes the highest combined burden from all state taxes and fees on Coloradans with low incomes and the middle class. Amendment ? lowers taxes for over 97 percent of Coloradans, including over 92 percent of taxpayers with income from business ownership. Taxpayers with over $200,000 in income pay roughly 3.9 percent of their income in state taxes and fees, the lowest rate of any income group, while taxpayers in the bottom half of the income distribution pay 4.7 percent. The measure asks that those who benefit the most from our state's economy contribute the most to maintaining the systems that support it.

Arguments Against Amendment ?

1) Amendment ? is a $2.0 billion tax increase on households and business owners. Those whose taxes will increase under the measure already pay the most taxes under the current system. The measure nearly doubles the state's top tax rate, raising it from among the lowest in the country to the sixth highest. Further, the COVID-19 crisis has already sent the economy into a deep recession. The measure worsens these impacts, hiking taxes for small business owners trying to keep workers on payrolls while leaving tax rates for many large corporations unchanged. A tax increase is economically risky at any time and especially dangerous when the economy is just beginning to recover.

2) Amendment ? lacks accountability to taxpayers. The measure raises taxes by twice the amount it requires to be spent on education, with no meaningful guardrails on how the remaining revenue will be used. The vague requirement that the state spend the remaining revenue "to address the impacts of a growing population and a changing economy" does not tell voters what programs or services will be funded. In effect, the measure allows the state to spend this money on nearly any part of the government without future input from voters. If voters are being asked to approve higher taxes, they should be given a clear explanation as to why the increase is necessary and where new funds will be spent.

Estimate of Fiscal Impact for Amendment ?

Estimates for the measure's effects on state revenue, state spending, and taxes are provided below. These estimates were required to be prepared in February 2020 for inclusion in the ballot question, prior to the COVID-19 pandemic. Because economic conditions have worsened in the months following preparation of the estimates, the actual amounts by which revenue, spending, and taxes will increase are expected to fall short of the amounts estimated here. These amounts will depend on the speed of the economic recovery and its effects on taxpayers of different income levels. If approved, Amendment ? would allow the state to retain and spend the new revenue generated by the graduated income tax in the measure, up to $2.0 billion, in state budget year 2021-22.

State revenue. Amendment ? is estimated to increase state revenue from income taxes by up to $1.0 billion in state budget year 2020-21, and up to $2.0 billion in state budget year 2021-22.

State spending. Amendment ? requires that at least half of the revenue it generates be spent on P-12 public education, and that the remainder be spent “to address the impacts of a growing population and a changing economy.” The state legislature will determine how to spend these funds.

Taxpayer impacts. Total state income taxes paid are estimated to increase by up to $2.0 billion in tax year 2021 under Amendment ?. The change in tax owed will depend on a taxpayer’s Colorado taxable income. On average, individual income taxpayers are estimated to pay an additional $646 for the year. Income tax owed is estimated to decrease by an average of $20 for those with taxable income below $255,275, and to increase by an average of $18,521 for those with taxable income over $255,275.