Office of Legislative Legal Services

Colorado General Assembly

Colorado State Capitol
200 East Colfax Avenue Suite 091
Denver, Colorado 80203-1716

Tel: 303-866-2045 Fax: 303-866-4157
Email: olls.ga@state.co.us

MEMORANDUM[1]

TO: Statutory Revision Committee

FROM: Pierce Lively, Office of Legislative Legal Services

DATE: January 9, 2020

SUBJECT: Repeal of the income tax deduction for previously taxed income or gain for C corporations

Summary

Section 39-21-305, C.R.S., requires the Office of the State Auditor (OSA) to evaluate all of the state's tax expenditures every five years. The OSA began to publish its evaluations of these tax expenditures in September 2018. The Tax Expenditure Evaluation Interim Study Committee (committee) convened during the 2019 legislative interim to review the policy considerations in the OSA's tax expenditure evaluations.

The OSA's evaluation of the income tax deduction for previously taxed income or gain for C corporations (deduction) found that it is extremely unlikely that anyone could qualify for this deduction. Therefore, the OSA's evaluation stated that the General Assembly may want to repeal the deduction.

After reviewing the OSA's evaluation of the exemption, the committee requested a draft of a bill repealing the deduction. The Office of Legislative Legal Services (OLLS) prepared the bill draft and informed the committee that the drafted bill fit within the

[1] This legal memorandum was prepared by the Office of Legislative Legal Services (OLLS) in the course of its statutory duty to provide staff assistance to the Statutory Revision Committee (SRC). It does not represent an official legal position of the OLLS, SRC, General Assembly, or the state of Colorado, and is not binding on the members of the SRC. This memorandum is intended for use in the legislative process and as information to assist the SRC in the performance of its legislative duties.

Statutory Revision Committee's (SRC) charge. The committee then unanimously requested that OLLS present the proposed bill to the SRC.

Analysis

The income tax deduction for previously taxed income or gain for C corporations should be repealed.

The deduction is codified in section 39-22-304 (3)(e)(I), C.R.S, and reads as follows:

> **39-22-304. Net income of corporation – legislative declaration – definitions - repeal.** (3) There shall be subtracted from federal tax income: (e)(I) The amount necessary to prevent the taxation under this article of any annuity or other amount of income or gain which was properly included in income or gain and was taxed under the laws of this state, for a taxable year prior to January 1, 1965, to the taxpayer, or to a decedent by reason of who death the taxpayer acquired the right to receive the income or gain, or to trust or estate from which the taxpayer received the income.

Under the deduction, C corporations, when calculating their Colorado taxable income, may deduct from their federal taxable income any income or gain that was taxed by Colorado prior to 1965, to the extent that such income or gain is included in their current federal taxable income. However, to claim this deduction, a C corporation must include the income or gain it intends to deduct in its current federal taxable income, and the C corporation must have been taxed by Colorado on the same income or gain prior to 1965. Therefore, it is unlikely that any C corporation could currently claim this deduction.

Statutory Charge[2]

The SRC is tasked with both examining Colorado statutes to discover "anachronisms in the law" and with recommending legislation "to effect such changes in the law as

[2] The Statutory Revision Committee is charged with "[making] an ongoing examination of the statutes of the state and current judicial decisions for the purpose of discovering defects and anachronisms in the law and recommending needed reforms" and recommending "legislation annually to effect such changes in the law as it deems necessary in order to modify or eliminate antiquated, redundant, or contradictory rules of law and to bring the law of this state into harmony with modern conditions." § 2-3-902 (1), C.R.S. In addition, the Committee "shall propose legislation only to streamline, reduce, or repeal provisions of the Colorado Revised Statutes." § 2-3-902 (3), C.R.S.

[the SRC] deems necessary in order to modify or eliminate antiquated … rules of law." Thus, removing the income tax deduction for previously taxed income or gain for C corporations appears to fall squarely within the SRC's charge because doing so eliminates an anachronism and an antiquated rule of law.

Proposed Bill

The attached bill only allows the income tax deduction for previously taxed income or gain for C corporations to be claimed for tax years prior to January 1, 2021.[3]

[3] The Taxpayer Bill of Rights requires that no "new state definition of taxable income shall apply before the next tax year," Colo. Const., art. X, § 20, thus the exemption cannot be repealed before the beginning of the first full tax year after the bill is signed into law.