MASS TRANSIT AND RIDESHARING EXPENSES DEDUCTION

EVALUATION SUMMARY | JANUARY 2021 | 2021-TE7

TAX TYPE	Corporate income
YEAR ENACTED	1979
REPEAL/EXPIRATION DATE	None
REVENUE IMPACT	Could not determine
NUMBER OF TAXPAYERS	Could not determine

KEY CONCLUSION: The deduction has not likely encouraged employers to offer mass transit and ridesharing options to employees because it was generally not usable prior to Tax Year 2018 and has likely not been used much since then due to a lack of awareness. Additionally, it may not provide a large enough benefit to induce a change in taxpayer behavior for most employers.

WHAT DOES THIS TAX EXPENDITURE DO?

The Mass Transit and Ridesharing Expenses Deduction allows corporate employers to deduct expenses for mass transit or ridesharing arrangements that they provide for employees from their Colorado taxable income.

WHAT IS THE PURPOSE OF THIS TAX EXPENDITURE?

Statute and the enacting legislation do not state the deduction's purpose; therefore, we could not definitively determine the General Assembly's original intent. Based on our review of legislative history and historical context, our evaluation considered a potential purpose: to encourage employers to offer mass transit and ridesharing options to employees by providing a financial benefit to employers that incur expenses for these options.

WHAT POLICY CONSIDERATIONS DID THE EVALUATION IDENTIFY?

The General Assembly may want to consider:

- Establishing a statutory purpose and performance measures for the deduction.
- Reviewing whether the deduction is meeting its intent and, if necessary, revise statute in order for the deduction to do so.

MASS TRANSIT AND RIDESHARING EXPENSES DEDUCTION

EVALUATION RESULTS

WHAT IS THE TAX EXPENDITURE?

Under the Mass Transit and Ridesharing Expenses Deduction (Mass Transit Expenses Deduction) [Section 39-22-509(1), C.R.S.], a corporate employer may deduct contributions they make to mass transit or ridesharing arrangements for employees from their Colorado taxable income. However, because Colorado uses federal taxable income as the starting point for determining Colorado taxable income, employers may only claim the deduction to the extent that they have not previously deducted eligible expenses when calculating their federal taxable income. In order for amounts to be eligible for the deduction, the mass transit or ridesharing arrangement must be primarily used to travel to and from an employee's workplace. In addition, for the purposes of the deduction, an eligible "ridesharing arrangement" is one in which people travel in a vehicle together with a commonality of purposes, provided that the vehicle is not operated for profit, which includes carpools and vanpools. Furthermore, statute provides that the deduction is available to "corporate employers," and Department of Revenue staff have interpreted this phrase to indicate C-corporations, including any entity that has made an election to be treated as a C-corporation for federal tax purposes.

Employers claim the Mass Transit Expenses Deduction on Line 13 of the Colorado C-Corporation Income Tax Return (Form DR 0112). The deduction was created by Senate Bill 79-001 in 1979 and has remained largely unchanged since then.

WHO ARE THE INTENDED BENEFICIARIES OF THE TAX EXPENDITURE?

Statute does not directly state the intended beneficiaries of the Mass Transit Expenses Deduction. Based on our review of the statutory language, we considered the intended beneficiaries to be corporations in Colorado that incur expenses for mass transit or ridesharing benefits they provide to employees.

WHAT IS THE PURPOSE OF THE TAX EXPENDITURE?

Statute and the enacting legislation for the Mass Transit Expenses Deduction do not state its purpose; therefore, we could not definitively determine the General Assembly's original intent. Based on our review of legislative history and historical context, we considered a potential purpose: to encourage employers to offer mass transit and ridesharing options to employees by providing a financial benefit to employers that incur expenses for these options. Specifically, the deduction was enacted alongside a number of other provisions that appear to be designed to encourage the increased use of alternative transportation options in lieu of single-occupancy vehicles. Additionally, national and local news articles indicate that policymakers and the public were increasingly interested in alternative transportation options when the enacting legislation was passed due to a number of recent trends, including the energy crises of 1974 and 1979, increases in gas prices paired with inflation, and concerns about air pollution.

IS THE TAX EXPENDITURE MEETING ITS PURPOSE AND WHAT PERFORMANCE MEASURES WERE USED TO MAKE THIS DETERMINATION?

We could not definitively determine whether the Mass Transit Expenses Deduction is meeting its purpose because no purpose is provided for it in statute or its enacting legislation. However, we found that it is not likely meeting the potential purpose that we identified in order to conduct this evaluation because it is not likely that many taxpayers are using the deduction.

Statute does not provide quantifiable performance measures for this deduction. Therefore, we created and applied the following performance measures to determine the extent to which the deduction is meeting its potential purpose:

PERFORMANCE MEASURE #1: *To what extent has the Mass Transit Expenses Deduction provided financial support to employers that incur expenses for mass transit and ridesharing options provided to employees?*

RESULT: We determined that the Mass Transit Expenses Deduction has not likely provided financial support to employers in recent years because the deduction was generally unusable for corporations prior to 2018. Additionally, awareness of the deduction appears to be relatively low, indicating that the deduction has not likely been used much between 2018 and the present, although the Department of Revenue lacked information to allow us to quantify its use.

Prior to 2018, the Mass Transit Expenses Deduction was generally not usable because employers could claim a federal income tax deduction for transportation benefits they provided employees under the Internal Revenue Code [26 U.S. Code, Section 162(a)(1)], which allows businesses to deduct all ordinary and necessary business expenses, including employee salaries and other forms of compensation. The Mass Transit Expenses Deduction allows expenses to be deducted only to the extent that they were not previously deducted when calculating federal taxable income. As a result, employers would have been able to deduct all of their expenses for employees' mass transit and ridesharing costs under the federal deduction and, thus, would not have been able to claim the Mass Transit Expenses Deduction when the federal deduction was available.

Beginning in 2018, due to changes to the Internal Revenue Code made through the 2017 Tax Cuts and Jobs Act, employers could no longer deduct most mass transit or ridesharing expenses they paid on behalf of employees when calculating their federal taxable income. As a result, these employers have been able to claim the Mass Transit Expenses Deduction for most eligible expenses since 2018. However, we found that awareness of the Mass Transit Expenses Deduction appears to be low; therefore, the deduction may not have been claimed by many employers even after the federal deduction was no longer available beginning in 2018. Specifically, none of the Colorado transit agencies that we consulted were aware of the deduction, including those that regularly have contact with employers and had informed employers about the federal deduction when it was available. We also attempted to contact businesses that may have been aware of the deduction. Most of these businesses did not respond, and those that did were either unaware of the deduction or had not incurred expenses to which the deduction would apply.

PERFORMANCE MEASURE #2: *To what extent has the Mass Transit Expenses Deduction increased the mass transit and ridesharing options available to employees at Colorado businesses?*

RESULT: The Mass Transit Expenses Deduction has not likely expanded the mass transit and ridesharing options available to employees at Colorado businesses because it is not likely being used much, as discussed in Performance Measure #1. Additionally, there are other savings programs available to some Colorado employers that likely provide a more substantial financial benefit than the deduction. For example, we estimated that the EcoPass program, which allows employers to purchase RTD transit passes for their employees at a discounted rate, could have saved employers between $953 and $1,817 per employee in 2018. In comparison, as discussed below, we estimate that the deduction could save employers $50 to $87 per employee per year. Although employers may benefit from these savings programs and the deduction simultaneously, the larger financial benefits provided by the savings programs that we identified indicate that these programs are more likely than the deduction to influence businesses' decisions on whether to offer mass transit options for employees.

WHAT ARE THE ECONOMIC COSTS AND BENEFITS OF THE TAX EXPENDITURE?

We determined that the Mass Transit Expenses Deduction likely had no revenue impact in 2017 because the deduction was generally not usable in 2017 or in previous years when expenses for employees' transportation were allowed to be deducted from the employer's income under federal law. We were unable to estimate the deduction's revenue impact in 2018 and 2019 due to a lack of Department of Revenue data and because publicly available data on mass transit fares does not include information about amounts paid by employers. In addition, we did not have sufficient information to determine how many, if any, employers are aware of the deduction and may have claimed it. The revenue impact in these years was probably minimal because taxpayer awareness of the deduction appears to be low.

However, if awareness of the deduction increases in future years and more employers begin claiming it on their income tax returns, the deduction's impact to state revenue could increase substantially. For example, if all employers that purchased transit passes for employees via RTD's EcoPass program in 2018 had paid for these expenses in full and claimed the deduction, we estimate that the deduction could have resulted in more than $1 million in forgone state revenue. This estimate does not include any amounts that Colorado employers could have claimed for expenses incurred through other transit agencies in the state, which would further increase the revenue impact.

WHAT IMPACT WOULD ELIMINATING THE TAX EXPENDITURE HAVE ON BENEFICIARIES?

Eliminating the Mass Transit Expenses Deduction would not likely have a significant impact on most taxpayers, since awareness of the deduction seems to be low. However, it would increase the income tax liabilities of employers that incur expenses for providing mass transit or ridesharing options and would otherwise have claimed the deduction for these expenses. Specifically, employers would be liable for corporate income tax on amounts they spent for these alternative transportation options, incurring income tax liabilities equal to 4.55 percent of these expenses (based on the Colorado income tax rate for Tax Year 2021).

As shown in EXHIBIT 1, based on 2018 transit costs, we estimated that Colorado employers that claim the deduction for purchases of monthly mass transit passes for employees could incur between $50 and $87 in additional annual corporate income tax liability per employee if the deduction were eliminated. For a Colorado employer with 14 employees (the statewide average number of employees per employer in 2018), this would amount to $700 to $1,218 in additional income tax liability.

EXHIBIT 1. ESTIMATED IMPACT OF MASS TRANSIT EXPENSES DEDUCTION TO AVERAGE COLORADO EMPLOYER[1], 2021

	Minimum	Maximum
Estimated average cost of one monthly transit pass in Colorado, 2018[2]	$92	$159
Total estimated annual cost of one monthly transit pass in Colorado, 2018	$1,104	$1,908
Colorado corporate income tax rate, 2021	4.55%	
= Estimated annual impact of deduction to employers, per employee, 2021	$50	$87
x Average number of employees per Colorado employer, 2018	14	
= Estimated impact of deduction to average Colorado employer, 2021	$700	$1,218

SOURCE: Office of the State Auditor analysis of Section 39-22-509(1), C.R.S., data from the United States Census Bureau and the National Transit Database, and information from Colorado transit agencies' websites and financial reports.
[1]For purposes of these calculations, we assumed that the employer paid 100 percent of the expenses incurred for each employee to have a monthly transit pass throughout 2018.
[2]We calculated the average cost of a monthly transit pass in Colorado based on transit agency ridership data from the National Transit Database and fare information on transit agencies' websites. If 2018 fares were not available for a given transit service, we used current fares instead.

Finally, based on feedback from Colorado transit agencies and businesses, we determined that awareness of the Mass Transit Expenses Deduction is fairly low. Eliminating the deduction would have no impact – financial or otherwise – on employers that would not have claimed the deduction because they were unaware of it. However, a transit agency indicated that the deduction may be a useful tool in their future conversations with businesses looking to purchase mass transit options for their employees; if the deduction were eliminated, this would no longer be the case.

ARE THERE SIMILAR TAX EXPENDITURES IN OTHER STATES?

We identified six states with tax expenditures similar to Colorado's Mass Transit Expenses Deduction, all of which allow employers to claim a credit or deduction for expenses incurred for providing alternative group transportation options to employees: California, Connecticut, Delaware, Maryland, Minnesota, and Washington. These tax expenditures may be claimed against various business income or similar taxes in all six states and may also be claimed against individual income taxes in Maryland and Minnesota. As demonstrated in EXHIBIT 2, other states' tax expenditures' benefits to taxpayers as a percentage of allowable costs are generally larger than Colorado's and range from about 9 percent to 50 percent of allowable expenses. Additionally, Connecticut, Delaware, and Washington all limit the statewide benefit to taxpayers resulting from their credits to $1.5 million, $100,000, and $2.75 million, respectively.

EXHIBIT 2. COMPARISON OF COLORADO'S MASS TRANSIT EXPENSES DEDUCTION AND SIMILAR TAX EXPENDITURES AVAILABLE IN OTHER STATES

State	Allowable Expenses		Benefit to Taxpayer as a Percentage of Allowable Costs	Annual Cap on Benefit Amount, per Employee
	Mass Transit?	Employer Ridesharing Program?		
Colorado	Yes	Yes	4.55%	None
California	Yes	Yes	8.84% [1]	None
Connecticut	Expenses for approved employer-sponsored traffic reduction programs[2]		50%	$250
Delaware	Yes	Yes	10% OR the percentage of employees benefitting from the program[3]	$250, if benefit based on percentage of employees benefitting
Maryland	Yes	Yes	50%	$1,200
Minnesota	Yes	No	30%	None
Washington	Yes	Yes	50%	$60

SOURCE: Office of the State Auditor analysis of other states' statutes, regulations, and official websites.

[1]California's tax expenditure is taken as a deduction from the state's corporation tax, which is applied to the net income of most corporations at the rate of 8.84 percent.

[2]Connecticut's credit is only available to employers with at least 100 employees at a workplace that is located in a "severe nonattainment area," as designated by the Environmental Protection Agency, with respect to national ambient air quality standards.

[3]This is calculated as the number of employees participating in the program for at least 100 days during the tax year divided by the annualized number of employees reporting and departing from the workplace during peak hours.

ARE THERE OTHER TAX EXPENDITURES OR PROGRAMS WITH A SIMILAR PURPOSE AVAILABLE IN THE STATE?

Although we did not identify any similar tax expenditures, we identified three Colorado public transit agencies that offer discount programs for employers that provide mass transit options to employees. Employers must obtain approval from the transit agency prior to purchasing passes at the reduced rate and must also meet certain minimum purchase requirements. As demonstrated in EXHIBIT 3, we estimated that employers could save between 15 percent and 87 percent on the costs of mass transit passes for employees as a result of participating in these programs. However, employers' actual savings would depend on the extent to which they would have purchased transit passes without the programs' availability and the extent to which they may pass on the cost of the transit passes to their employees. Finally, any expenses incurred by employers purchasing passes through these programs would likely be eligible for the Mass Transit Expenses Deduction.

EXHIBIT 3. EMPLOYER SAVINGS PROGRAMS OFFERED BY COLORADO TRANSIT AGENCIES

Transit Agency and Employer Program	Minimum Required Purchase	Percent Saved from Employer Program[1]
RTD: EcoPass (Denver metro area)	Employers must purchase passes for all full-time employees.	77% - 87%[2]
Transfort: PassFort (Fort Collins)	Businesses with no more than 25 employees must purchase passes for all employees. Businesses with more than 25 employees must purchase at least 25 passes.	68%
ECO Transit: Employer bulk pass purchase discount (Eagle County)	5 passes	15%

SOURCE: Office of the State Auditor analysis of Regional Transportation District data and information from transit agency websites.
[1]These percentages are calculated under the assumption that employers would purchase the same number of passes regardless of whether they actually participated in the program and received the program's discounts. Actual savings may be less than the percentages presented here as a result of this. Additionally, the calculations do not include any savings that employers may receive if they claim the expenses incurred under the Mass Transit Expenses Deduction for corporate income tax purposes.
[2]Estimates of EcoPass savings are based on 2019 data.

WHAT DATA CONSTRAINTS IMPACTED OUR ABILITY TO EVALUATE THE TAX EXPENDITURE?

The Department of Revenue was not able to provide us with data on the number of taxpayers that claimed the Mass Transit Expenses Deduction or the amounts claimed. Specifically, the deduction is not itemized on the Colorado C-Corporation Income Tax Return (Form DR 0112). As a result, taxpayers claim the deduction on the "Other subtractions" lines of this return, which combines several other deductions and cannot be disaggregated for analysis. To address this limitation, the Department could create a new reporting line for the deduction on the income tax return. Additionally, the Department would need to capture and house the data collected on the new line in GenTax, which would also require additional resources (see the Tax Expenditures Overview Section of the Office of the State Auditor's *Tax Expenditures Compilation Report* for additional details on the limitations of Department of Revenue data and the potential costs of addressing the limitations).

WHAT POLICY CONSIDERATIONS DID THE EVALUATION IDENTIFY?

THE GENERAL ASSEMBLY MAY WANT TO CONSIDER AMENDING STATUTE TO ESTABLISH A STATUTORY PURPOSE AND PERFORMANCE MEASURES FOR THE MASS TRANSIT EXPENSES DEDUCTION. As discussed, statute and the enacting legislation for the deduction do not state the deduction's purpose or provide performance measures for evaluating its effectiveness. Therefore, for the purposes of our evaluation, we considered a potential purpose for the deduction: to encourage employers to offer mass transit and ridesharing options to employees by providing a financial benefit to employers that incur expenses for these options. We identified this purpose based on our review of the following sources:

- LEGISLATIVE HISTORY. The Mass Transit Expenses Deduction was passed as part of a larger bill [Senate Bill 79-001] that primarily addressed concerns regarding motor vehicle emissions. In addition to the Mass Transit Expenses Deduction, several other provisions in this bill seem to have been designed to encourage increased use of alternative transportation in lieu of single-occupancy vehicles. For example, the bill established preferential off-street parking rates for vehicles used by more than one person going to or from work and allowed non-State employees to fill vacant spaces in State-owned vanpools for a monthly fee.

- HISTORICAL CONTEXT. National and local news articles published around the time that the deduction was enacted indicate that there was an increased interest in alternative transportation among legislators and the public at this time. These articles cited a number of reasons for this increased interest, including the energy crises of 1974 and 1979, increases in gas prices paired with inflation, and concerns about air pollution.

We also developed two performance measures to assess the extent to which the deduction is meeting its potential purpose. However, the General Assembly may want to clarify its intent for the deduction by providing a purpose statement and corresponding performance measure(s) in statute. This would eliminate potential uncertainty regarding the deduction's purpose and allow our office to more definitively assess the extent to which the deduction is accomplishing its intended goal(s).

THE GENERAL ASSEMBLY MAY WANT TO REVIEW WHETHER THE MASS TRANSIT EXPENSES DEDUCTION IS MEETING ITS INTENT AND, IF NECESSARY, REVISE STATUTE IN ORDER FOR THE DEDUCTION TO DO SO. As discussed, we identified a number of factors that may limit the extent to which the deduction is meeting the potential purpose that we identified for this evaluation:

- THE DEDUCTION HAS LIKELY NOT BEEN USED MUCH, IF AT ALL, IN RECENT YEARS. We determined that awareness of the Mass Transit Expenses Deduction is low among transit agencies and businesses, indicating that the deduction has not likely been used much in recent years. Additionally, prior to 2018, employers would have been able to deduct all of their expenses for employees' mass transit and ridesharing costs as ordinary and necessary business expenses when calculating federal taxable income. Therefore, employers would not have been able to claim the Mass Transit Expenses Deduction until 2018, when most expenses for employee transportation were no longer allowed to be deducted under federal law.

- THE DEDUCTION'S BENEFIT MAY NOT BE LARGE ENOUGH TO INDUCE A CHANGE IN TAXPAYER BEHAVIOR FOR MOST EMPLOYERS, especially since there are other programs that provide much larger benefits to employers seeking to reduce the costs of providing mass transit options to employees. For example, we estimated that the EcoPass program, which allows employers to purchase RTD transit passes for their employees at a discounted rate, could have saved employers between 77 percent and 87 percent on these expenses in 2019 compared with the 4.55 percent savings employers would receive from the deduction for Tax Year 2021. Additionally, the tax savings provided by the deduction is much smaller than the savings provided by comparable tax expenditures that we identified in six other states, which provide savings between 9 percent and 50 percent of eligible expenses incurred.

We also identified several other considerations that the General Assembly may want to take into account if it decides to review the deduction for potential revision:

- THE DEDUCTION'S REVENUE IMPACT HAS LIKELY BEEN SMALL BUT MAY INCREASE. We determined that the deduction likely had no revenue impact in 2017, and though we were unable to estimate the deduction's revenue impact in 2018 and beyond due to a lack of available data, the impact was likely still minimal due to a lack of awareness of the deduction. However, if more employers begin claiming the deduction in future years, its impact to state revenue could increase substantially. For example, if all employers that purchased transit passes for employees via RTD's EcoPass program in 2018 had paid for these expenses in full and claimed the deduction, we estimated that the deduction would have resulted in over $1 million in forgone revenue to the State.

- THE DEFINITION OF "RIDESHARING" FOR THE PURPOSES OF THE DEDUCTION MAY BE OBSOLETE. The deduction has not been substantively revised since its enactment in 1979, and transportation patterns have changed since then. For example, part of the definition of "ridesharing arrangement" for purposes of the deduction appears to be targeted towards private ridesharing programs that are established by employers specifically for their employees' commuting needs. Although we were unable to determine how common private ridesharing programs are among Colorado employers, ridesharing trips accounted for only 0.3 percent of total paid public transit trips in Colorado in 2018, which may indicate that private ridesharing programs are less common now than they were in the past. Additionally, more modern forms of ridesharing, such as Uber Pool and Lyft Shared rides, are not likely to be allowable under the deduction because the deduction requires that the ridesharing arrangement not be operated for profit by a transportation business.