

COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 5225H.011
 Bill No.: HB 2460
 Subject: Political Subdivisions; Taxation and Revenue - Income; Cities, Towns, and Villages; Counties
 Type: Original
 Date: January 29, 2024

Bill Summary: This proposal modifies provisions governing income exempt from earnings tax.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND			
FUND AFFECTED	FY 2025	FY 2026	FY 2027
General Revenue	More or Less than \$30,347	More or Less than \$91,040	More or Less than \$91,040
Total Estimated Net Effect on General Revenue	More or Less than \$30,347	More or Less than \$91,040	More or Less than \$91,040

ESTIMATED NET EFFECT ON OTHER STATE FUNDS			
FUND AFFECTED	FY 2025	FY 2026	FY 2027
Total Estimated Net Effect on <u>Other</u> State Funds	\$0	\$0	\$0

Numbers within parentheses: () indicate costs or losses.

ESTIMATED NET EFFECT ON FEDERAL FUNDS			
FUND AFFECTED	FY 2025	FY 2026	FY 2027
Total Estimated Net Effect on <u>All</u> Federal Funds	\$0	\$0	\$0

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)			
FUND AFFECTED	FY 2025	FY 2026	FY 2027
Total Estimated Net Effect on FTE	0	0	0

- Estimated Net Effect (expenditures or reduced revenues) expected to exceed \$250,000 in any of the three fiscal years after implementation of the act or at full implementation of the act.
- Estimated Net Effect (savings or increased revenues) expected to exceed \$250,000 in any of the three fiscal years after implementation of the act or at full implementation of the act.

ESTIMATED NET EFFECT ON LOCAL FUNDS			
FUND AFFECTED	FY 2025	FY 2026	FY 2027
Local Government	More or Less than (\$2,233,245)	More or Less than (\$6,699,735)	More or Less than (\$6,699,735)

FISCAL ANALYSIS

ASSUMPTION

Oversight was unable to receive some of the agency responses in a timely manner due to the short fiscal note request time. Oversight has presented this fiscal note on the best current information that we have or on prior year information regarding a similar bill. Upon the receipt of agency responses, Oversight will review to determine if an updated fiscal note should be prepared and seek the necessary approval to publish a new fiscal note.

§92.130 – Income Exempt from Earnings Tax for Low-Income Taxpayers

Officials from the **Office of Administration - Budget and Planning (B&P)** assume this proposal would exempt citizen income from the earnings tax levied by St. Louis City and Kansas City, for individuals with income up to 150% of the federal poverty level.

B&P notes that this proposal would become effective August 28, 2024 – in the middle of tax year 2024. B&P further notes that while earnings tax returns are not due until January of the next year, many city residents have the 1% tax withheld from their paychecks. B&P assumes that the city would still collect (and retain) earnings tax on income earned through August 2024.

B&P further notes that the term “citizen” is not defined. It is unclear whether this term refers to city residents, state residents, or U.S. citizens. Due to data limitations, B&P can only estimate the impact from city residents; however, this term could encompass a much broader group of people.

In addition, this proposal sets the income level at “150% of the federal poverty level”. B&P notes that the federal poverty level is dependent on family size. It is unclear whether the term used here refers to the income limit for single people or whether household size should be used. Due to data limitations, B&P will estimate the impact based on the 150% FPL for singles. B&P notes that in 2023 that amount was \$21,870.

Kansas City and St. Louis City

Based on data published by the U.S. Census Bureau, B&P estimates that up to 22,216 residents of Kansas City, age 16 and up, could qualify for this exemption. In addition, up to 13,445 St. Louis City residents, age 16 and up, could qualify. Table 1 shows the resident county by income level.

Table 1: Residents by Income

<u>Income Level</u>	<u>Kansas City</u>	<u>St. Louis City</u>
\$1 to \$9,999 or less	3,305	1,750
\$10,000 to \$14,999	4,412	2,854
\$15,000 to \$24,999	14,499	8,841
Total	22,216	13,445

Using this data, B&P estimates that this proposal could exempt resident income up to \$416,315,413 from the Kansas City earnings tax and up to \$253,658,066 from the St. Louis City earnings tax.

Therefore, B&P estimates that this proposal could reduce Kansas City earnings tax collections by up to \$4,163,154 ($\$416,315,413 \times 1\%$) and St. Louis City earnings tax collections by \$2,536,581 ($\$253,658,066 \times 1\%$) annually. For tax year 2024 (FY25), B&P estimates that this could reduce Kansas City earnings taxes by \$1,387,718 (four months of collections). This could also reduce St. Louis City earnings tax collections by \$845,527 (four months of collections) for tax year 2024 (FY25).

General Revenue

B&P notes that some taxpayers claim the amount of earnings tax paid to St. Louis City in their itemized deductions. Based on 2021 tax return data (the most recent complete year available), B&P determined that 28.3% (rounded) of Missouri taxpayers itemize their deductions.

Therefore B&P estimates that \$632,219 ($(\$1,387,718 + \$845,527) \times 28.3\%$) in fewer deductions would be claimed for tax year 2024. Once fully implemented, B&P estimates that \$4,840,144 ($(\$4,163,154 + \$2,536,581) \times 28.3\%$) in fewer deductions would be claimed annually.

However, deductions do not reduce revenues on a dollar-for-dollar bases, but rather in proportion to the top tax rate applied. Therefore, B&P will show the estimated impact throughout the implementation of SB 3 (2022).

B&P assumes that this provision may increase TSR and GR by \$60,693 in FY25. Once SB 3 (2022) has fully implemented, this provision could increase TSR and GR by \$85,350 annually. Table 3 shows the estimated state GR impact for future years, through the implementation of SB 3 (2022).

Table 3: Estimated Revenue Gain by Fiscal Year

Tax Rate	Tax Year (Fiscal Year)			
	2024 (FY25)	2025 (FY26)	2026 (FY27)	2027 (FY28)
4.80%	\$30,347	\$91,040	\$91,040	\$91,040
4.70%		\$89,143	\$89,143	\$89,143
4.60%			\$87,246	\$87,246
4.50%				\$85,350

Officials from the **Department of Revenue (DOR)** assume this proposal will make changes to the earning tax that the City of Kansas City and the City of St. Louis assess. This proposal would allow “low-income” citizens an exemption from paying the earnings tax. A low-income citizen is defined as an individual who has an income at or below 150% of the federal poverty level. DOR notes that the federal poverty level is based on family size and income. It is unclear from this proposal if these cities are to calculate the poverty level on an individual or their family. The federal poverty income limit for an individual at 150% of the poverty level is \$21,870.

Additionally, this proposal does not make clear if “citizen” refers to city residents, state residents or U.S. citizen. For purposes of the fiscal note, DOR will assume it refers to the citizens that are residents of the city.

This proposal would become effective on August 28, 2024, in the middle of a tax year. Earnings tax is owed each year in January covering your earnings of the year before. Most people who pay the tax have money withheld throughout the year to pay the tax. DOR assumes that those who would no longer owe, would have the collection stopped on their income. Therefore, when this proposal starts, some citizens would no longer owe the tax.

Using information from the U.S Census Bureau, DOR estimates that 22,216 residents of Kansas City and 13,445 residents of St. Louis City ages 16 and up would no longer owe this tax. This table shows the resident county by income level.

Table 1: Residents by Income

<u>Income Level</u>	<u>Kansas</u>	
	<u>City</u>	<u>St. Louis City</u>
\$1 to \$9,999 or less	3,305	1,750
\$10,000 to \$14,999	4,412	2,854
\$15,000 to \$24,999	14,499	8,841
Total	22,216	13,445

Using the same data, DOR notes that this could exempt total income of \$416,315,413 in Kansas City and \$253,658,066 in St. Louis. Both citizens currently collect a 1% earnings tax so this would result in a loss of \$4,163,154 to Kansas City and \$2,536,581 to St. Louis City for a total of \$6,699,735 in tax year 2025. DOR notes this would reduce the tax year 2024 collections by four months.

When citizens pay the earnings tax and they itemize their MO individual income tax return, they are allowed a deduction of the local tax paid. Therefore, any reduction in the amount paid to Kansas City or St. Louis would result in increased revenue to the general revenue fund.

Using DOR’s individual income tax data for the most complete year, tax year 2021, DOR determined that 28.3% of Missouri taxpayers itemize their deductions. Using that same 28.3% DOR assumes that \$718,092 ($\$2,536,581 * 28.3\%$) is itemized in St. Louis and \$1,178,566 ($\$4,163,154 * 28.3\%$) is itemized in Kansas City. This would result in \$1,896,658 increased revenue to general revenue in tax year 2025 with \$632,219 (4 months) in tax year 2024.

A deduction does not reduce revenue on a dollar-for-dollar basis, but rather in proportion to the highest tax rate. SB 3 will be phasing down the individual income tax from 4.8% to 4.5%. We will show the impact of this proposal throughout implementation of SB 3.

The impact to general revenue:

Table 3: Estimated Revenue Gain by Fiscal Year

Tax Rate	Tax Year (Fiscal Year)			
	2024 (FY25)	2025 (FY26)	2026 (FY27)	2027 (FY28)
4.80%	\$30,347	\$91,040	\$91,040	\$91,040
4.70%		\$89,143	\$89,143	\$89,143
4.60%			\$87,246	\$87,246
4.50%				\$85,350

This will require DOR to update our MO-1040 and MO-A form, our website and our computer programs. These changes are estimated at 8,923.

Oversight assumes DOR is provided with core funding to handle a certain amount of activity relating to the updating of tax forms each year. Oversight assumes DOR could absorb the costs related to this proposal. If multiple bills pass which require additional staffing and duties at substantial costs, DOR could request funding through the appropriation process.

Oversight does not have information to the contrary and therefore, Oversight will reflect the estimates as provided by the B&P and DOR.

Officials from the **Department of Labor and Industrial Relations** assume the proposal will have no fiscal impact on their organization. **Oversight** does not have any information to the contrary. Therefore, Oversight will reflect a zero impact in the fiscal note.

<u>FISCAL IMPACT – State Government</u>	FY 2025 (4 Mo.)	FY 2026	FY 2027
GENERAL REVENUE			
<u>Savings</u> – calculation of deductions relating to earnings tax that can no longer be itemized on state taxes §92.130	<u>More or Less than \$30,347</u>	<u>More or Less than \$91,040</u>	<u>More or Less than \$91,040</u>
ESTIMATED NET EFFECT ON GENERAL REVENUE	<u>More or Less than \$30,347</u>	<u>More or Less than \$91,040</u>	<u>More or Less than \$91,040</u>

<u>FISCAL IMPACT – Local Government</u>	FY 2025 (4 Mo.)	FY 2026	FY 2027
LOCAL POLITICAL SUBDIVISIONS			
<u>Revenue Loss</u> – potential loss in revenue from eliminating the Earnings Tax on Low-Income Taxpayers §92.130	<u>More or Less than (\$2,233,245)</u>	<u>More or Less than (\$6,699,735)</u>	<u>More or Less than (\$6,699,735)</u>
ESTIMATED NET EFFECT ON LOCAL POLITICAL SUBDIVISIONS	<u>More or Less than (\$2,233,245)</u>	<u>More or Less than (\$6,699,735)</u>	<u>More or Less than (\$6,699,735)</u>

FISCAL IMPACT – Small Business

No direct fiscal impact to small businesses would be expected as a result of this proposal.

FISCAL DESCRIPTION

This bill exempts from the city earnings tax all taxpayers whose income is at or below 150% of the federal poverty level.

This legislation is not federally mandated, would not duplicate any other program and would not require additional capital improvements or rental space.

L.R. No. 5225H.011

Bill No. HB 2460

Page 8 of 8

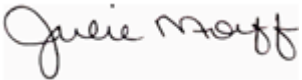
January 29, 2024

SOURCES OF INFORMATION

Office of Administration - Budget and Planning

Department of Revenue

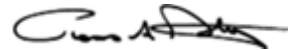
Department of Labor and Industrial Relations



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January 29, 2024



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