

COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 5974S.05F
 Bill No.: Perfected SS for SCS for SB Nos. 3 & 5
 Subject: Taxation and Revenue - Income
 Type: Original
 Date: September 20, 2022

Bill Summary: This proposal modifies provisions relating to income taxes.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND				
FUND AFFECTED	FY 2023	FY 2024	FY 2025	Fully Implemented (FY 2028)
General Revenue Fund *	(\$130,633,876)	(\$335,434,081)	(\$370,091,425)	(\$371,230,602)
Total Estimated Net Effect on General Revenue	(\$130,633,876)	(\$335,434,081)	(\$370,091,425)	(\$371,230,602)

*Oversight notes the state individual income tax rate (5.3% in CY 2022) is to be reduced in 0.10% annual increments (if certain triggers are met) until it reaches 4.8%. This proposal would change the tax rate to 4.95% starting January 1, 2023. This proposal also allows for an additional 0.15% GR-growth-dependent reduction in CY 2024 to 4.8%. Additionally, this proposal allows for an additional three 0.1% GR-growth-dependent reductions that could occur as early as CY 2025 (assuming the GR dependent trigger was met) until it reaches 4.5%. The impact for FY 2023 is smaller because it reflects a partial year. The fiscal note reflects the assumptions that the current triggers would have been met each year (would have reduced the rate to 4.8% regardless of this bill) and that the additional triggers in the bill will be met each year, occurring in CY 2024 – CY 2027.

ESTIMATED NET EFFECT ON OTHER STATE FUNDS				
FUND AFFECTED	FY 2023	FY 2024	FY 2025	Fully Implemented (FY 2028)
Total Estimated Net Effect on <u>Other</u> State Funds	\$0	\$0	\$0	\$0

Numbers within parentheses: () indicate costs or losses.

ESTIMATED NET EFFECT ON FEDERAL FUNDS				
FUND AFFECTED	FY 2023	FY 2024	FY 2025	Fully Implemented (FY 2028)
Total Estimated Net Effect on <u>All</u> Federal Funds	\$0	\$0	\$0	\$0

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)				
FUND AFFECTED	FY 2023	FY 2024	FY 2025	Fully Implemented (FY 2028)
Total Estimated Net Effect on FTE	0	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 2023	FY 2024	FY 2025	Fully Implemented (FY 2028)
Local Government	\$0	\$0	\$0	\$0

FISCAL ANALYSIS

ASSUMPTION

Oversight notes this proposal contains a Section B with an effective date for a designated section (143.011). That section would go into effect on January 1, 2023.

Oversight notes this proposal contains an emergency clause (Section C) that would make this proposal effective upon signing by the Governor for section 143.021. For the simplicity of the fiscal note, we will assume this provision would go into effect on October 1, 2022.

Sections 143.011 – 143.021 Individual Income Tax Rate

Officials from the **Department of Revenue (DOR)** noted in 2013 Missouri's individual income tax rate was 6% per the tax tables printed in statutes. In 2014, SB 509 then allowed for five reductions of the individual income tax rate based on certain revenue triggers (Section 143.011.2). The Department notes that currently three of those reductions have occurred (TY 2018, TY 2019 and TY 2022) and the fourth is forecasted to happen in tax year 2023, which will set the rate at 5.2%.

Additionally, in 2019, HB 2540 was added to statutes that caused the individual income tax rate to be decreased by four-tenths of one percent (Section 143.011.3). Then during the 101st General Assembly regular session SB 153 & 97 was passed that would allow starting in tax year 2024 another two reductions of SB 509 (Section 143.011.4). Therefore, as of the filing of the fiscal note the individual income tax rate for tax year 2022 is 5.3% and the tax rate scheduled for tax year 2023 is 5.2%.

This proposal in Section 143.011.2 adds language that would lower the individual income tax rate to 4.95% starting January 1, 2023. This proposal would then allow for another fifteen hundredths of a percent reduction in the individual income tax rate starting January 1, 2024 if a certain trigger is met. A reduction in the rate of tax shall only occur if the amount of net general revenue collected in the previous fiscal year exceeds the highest amount of net general revenue collected in any of the three fiscal years prior to such fiscal year by at least one hundred seventy-five million dollars.

Starting after the two previous reductions, this proposal will allow three additional reductions of one-tenth of one percent reductions in the individual income tax rate. No more than one reduction can be made annually and will only occur if three triggers are met. A reduction in the rate of tax shall only occur if:

- a. The amount of net general revenue collected in the previous fiscal year exceeds the highest amount of net general revenue collected in any of the three fiscal years prior to such fiscal year by at least two hundred million dollars; and

- b. The amount of net general revenue collected in the previous fiscal year exceeds the amount of net general revenue collected in the fiscal year five years prior, adjusted by the percentage increase in inflation over the preceding five fiscal years.

(b) The amount of net general revenue collected required by subparagraph a of paragraph (a) of this subdivision in order to make a reduction pursuant to this subsection shall be adjusted annually by the percent increase in inflation beginning with the effective date of this section.

This proposal also adds language that starting January 1, 2023, eliminates the current lowest tax bracket. This would make the lowest bracket start at \$1,000 instead of \$100.

For fiscal note purposes only, the Department shows the individual income tax reductions occurring in consecutive years. Using the Department's internal Income Tax Model that contains confidential taxpayer data, DOR was able to estimate the following impact of these new changes starting in tax year 2023.

Tax Year	Amount
2023	(\$309,618,774)
2024	(\$367,313,334)
2025	(\$369,576,908)
2026	(\$368,358,203)
2027	(\$370,662,102)

The Department uses a 42%/58% split when converting from tax years to fiscal years.

Fiscal Year	Loss to GR
2023	(\$130,039,885)
2024	(\$333,850,489)
2025	(\$368,264,035)
2026	(\$369,065,052)
2027	(\$369,325,840)
2028	(\$370,662,102)

This proposal will require computer upgrades, form changes and website changes. This is estimated at \$10,000 in one-time costs.

Oversight notes that DOR assumes this proposal will require programming changes estimated to cost \$10,000. **Oversight** assumes the Department of Revenue is provided with core funding to handle a certain amount of activity 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.

Officials from the **Office of Administration - Budget and Planning (B&P)** note Section 143.011 would reduce the top tax rate to 4.95% beginning with tax year 2023. This would also create an additional rate reduction of 0.15% as early as tax year 2024, depending on net general revenue growth. In order to trigger this reduction, net general revenue must grow by \$175 million over the largest of the three previous fiscal years.

In addition, as early as tax year 2025 three additional 0.1% reductions may occur, depending on net general revenue growth. In order to trigger these reductions, net general revenue must grow by at least \$200 million, adjusted for inflation, over the highest of the three previous fiscal years and net general revenue must be greater than the five-year inflation adjusted net general revenue.

Section 143.021 would eliminate the bottom individual income tax bracket.

B&P notes that under current law the top tax rate will be 5.2% starting with tax year 2023. B&P notes that per SB 153 (2021) there will be a 0.1% reduction in the top rate for tax year 2024. Based on current revenue forecasts and average revenue growth, B&P estimates that revenues in FY24, FY25, and FY26 will reach the growth trigger requirement for reductions to the top rate of tax. Therefore, the top rate of tax is estimated to be reduced by 0.1% in tax years 2025, 2026, 2027 under SB 509 (2014) and SB 153 (2021). For the purpose of this fiscal note, B&P will assume that the rate reductions created under this proposal will trigger for each tax year from 2024 through 2027. However, B&P acknowledges that it is unlikely that the reductions will trigger in consecutive years. Table 1 shows the current versus proposed top rate of tax.

Table 1: Current versus
Proposed Top Tax Rate

Tax Year	Current Law	Proposed
2023	5.20%	4.95%
2024	5.10%	4.80%
2025	5.00%	4.70%
2026	4.90%	4.60%
2027	4.80%	4.50%

Using tax year 2019 data, the most recent complete tax year available, and accounting for the changes in individual income tax law created by SB 509 (2014) and SB 153 (2021), B&P estimates that this proposal may reduce tax collections by \$311.0M in tax year 2023. Once this proposal fully implements, B&P estimates this provision could reduce tax collections by \$371.2M annually, compared to revenues under SB 509 (2014) and SB 153 (2021) with a top rate 4.8%. Table 2 shows the estimated revenue impact by tax year.

Table 2: Estimated
Impact by Tax Year

Tax Year	GR Impact
2023	(\$311,033,037)
2024	(\$369,130,762)
2025	(\$371,418,054)
2026	(\$370,204,431)
2027	(\$371,230,602)

However, because this proposal would take effect January 1, 2023, individuals will adjust their withholdings and declarations during FY23. Based on actual collections data, B&P estimates that 42% of individual income taxes are paid during fiscal year 1 and 58% are paid during fiscal year 2. Therefore, B&P estimates that this provision could reduce TSR and GR by \$130.6M in FY23. Once fully implemented, and annually thereafter, this proposal may reduce TSR and GR by \$371.2M, compared to revenues under SB 509 (2014) and SB 153 (2021) with a top rate 4.8%. Table 3 shows the estimated impact by fiscal year.

Table 3: Estimated Impact
by Fiscal Year

Fiscal Year	GR Impact
2023	(\$130,633,876)
2024	(\$335,434,081)
2025	(\$370,091,425)
2026	(\$370,908,333)
2027	(\$370,635,423)
2028	(\$371,230,602)

Oversight notes that under the current law, SB 509 (2014) and SB 153 (2021) allows for a top rate of 4.8% to be established by CY 2027, as shown below.

Oversight notes that this proposal reduces the top individual income tax rate to 4.95% beginning with the 2023 calendar year. This proposal allows an additional 0.15% GR-growth-dependent reduction in calendar 2024 to 4.8%. Finally, Oversight notes this proposal also allows for an additional three tenths of the percentage decline after the State reaches the 4.8% tax top rate. Each year, for purpose of this fiscal note, the additional trigger would be met to show the greatest impact to the general revenue as shown below:

Tax Year	Current Law	Proposed Law	Effect
2023	5.20%	4.95%	Proposed top individual income tax rate
2024	5.10%	4.80%	Proposed fifteen hundredths of a percent reduction
2025	5.00%	4.70%	Proposed one-tenth of a Percent reduction (Dependent on GR growth)
2026	4.90%	4.60%	Proposed one-tenth of a Percent reduction (Dependent on GR growth)
2027	4.80%	4.50%	Proposed one-tenth of a Percent reduction (Dependent on GR growth)

Oversight notes both DOR and B&P’s estimates include data from DOR and B&P’s internal Income Tax Model. Additionally, **Oversight** notes both DOR and B&P’s estimates of revenue impact assume all scheduled rate reductions will occur.

Oversight notes that it does not currently have the resources and/or access to state tax data to produce a thorough independent revenue estimate and is unable to verify the revenue estimates provided by B&P and DOR. Therefore, for the purpose of this fiscal note, Oversight will note B&P’s estimated impact for this proposal.

Oversight notes the senate substitute provided two word changes to the bill language and does not change the fiscal impact of the bill.

<u>FISCAL IMPACT – State Government</u>	FY 2023 (10 Mo.)	FY 2024	FY 2025	Fully Implemented (FY 2028)
GENERAL REVENUE FUND				
<u>Revenue Loss - §143.011 - §143.021 Individual Income Tax p.3-7</u>	(\$130,633,876)	(\$335,434,081)	(\$370,091,425)	(\$371,230,602)
ESTIMATED NET EFFECT ON GENERAL REVENUE FUND	(\$130,633,876)	(\$335,434,081)	(\$370,091,425)	(\$371,230,602)

<u>FISCAL IMPACT – Local Government</u>	FY 2023 (10 Mo.)	FY 2024	FY 2025	Fully Implemented (FY 2028)
	\$0	\$0	\$0	\$0

FISCAL IMPACT – Small Business

Certain small businesses may pay less in income tax as a result of this proposal.

FISCAL DESCRIPTION

Current law provides for reductions to the top rate of income tax to an eventual rate of 4.8% over a period of years, contingent on meeting certain net general revenue collection triggers. This act repeals all such scheduled reductions and reduces the top rate of income tax to 4.95% beginning in the 2023 calendar year. This act also adds one additional potential 0.15% reduction in the top rate of tax. Such additional reduction shall only be effective if the amount of net general revenue collected in the previous fiscal year exceeds the highest amount of net general revenue collected in any of the three fiscal years prior to such fiscal year by at least \$175 million. Finally, this act adds three additional potential 0.1% reductions in the top rate of tax, for an eventual rate of 4.5%. Such additional reductions shall only be effective if the amount of net general revenue collected in the previous fiscal year exceeds the highest amount of net general revenue collected in any of the three fiscal years prior to such fiscal year by at least \$200 million, and exceeds the amount of net general revenue collections from the fifth prior fiscal year, adjusted for inflation. The amount of net general revenue collected required to reduce the top rate of tax from 4.8% to 4.5% shall be adjusted annually by the percent increase in inflation. (Section 143.011)

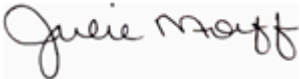
Current law exempts the first \$100 of a taxpayer's income from taxation. For all tax years beginning on or after January 1, 2023, this act exempts the first \$1,000 of income from taxation. (Section 143.021)

This act contains an emergency clause.

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

SOURCES OF INFORMATION

Department of Revenue
Office of Administration - Budget and Planning



Julie Morff
Director
September 20, 2022



Ross Strobe
Assistant Director
September 20, 2022