

COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 4100-01
Bill No.: HB 1426
Subject: Taxation and Revenue - Income; Higher Education
Type: Original
Date: February 24, 2004

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND			
FUND AFFECTED	FY 2005	FY 2006	FY 2007
General Revenue	\$0	(\$12,381,098)	(\$24,629,788)
Total Estimated Net Effect on General Revenue Fund	\$0	(\$12,381,098)	(\$24,629,788)

ESTIMATED NET EFFECT ON STATE FUNDS			
FUND AFFECTED	FY 2005	FY 2006	FY 2007
Total Estimated Net Effect on <u>All</u> State Funds	\$0	\$0	\$0

Numbers within parentheses: () indicate costs or losses.
This fiscal note contains 6 pages.

ESTIMATED NET EFFECT ON FEDERAL FUNDS
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FUND AFFECTED	FY 2005	FY 2006	FY 2007
Total Estimated Net Effect on <u>All</u> Federal Funds	\$0	\$0	\$0

ESTIMATED NET EFFECT ON LOCAL FUNDS			
FUND AFFECTED	FY 2005	FY 2006	FY 2007
Local Government	\$0	\$0	\$0

FISCAL ANALYSIS

ASSUMPTION

Officials from the **Department of Revenue (DOR)** assume this legislation exempts from taxation all income earned by any graduate who permanently resides in this state and who is employed by a company located in this state. The exemption provided in this section applies to the three consecutive tax years beginning on or after January 1st of the year immediately following the date the graduate receives the degree. DOR is to promulgate rules and regulations.

Graduate means any person who completes a program of study for which the person receives a masters or doctoral degree from any public or private university located in this state. The term graduate shall not include any person who receives any degree from any school of law or school of medicine.

Personal Tax will handle this as a Missouri modification (at least for married filing combined taxpayers where one of the individuals is not a graduate). If a single graduate taxpayer does not file a return with DOR due to the exemption of income from taxes, DOR will not be able to identify them on any of DOR's match programs (IRS with Missouri address) or warehouse items. So DOR will require these graduates file a return and take the income as an adjustment or deal with all of the non-filer notices.

ASSUMPTION (continued)

Personal Tax will need 2 Tax Season Temporaries for every 50,000 returns and 1 Tax Processing Tech I for every 15,000 errors created by this legislation. Personal Tax will also need 1 Tax Processing Tech I for every additional 3,000 pieces of correspondence.

DOR assumes the Form MO-A will need to be modified for this deduction. MINITS mainframe system will need to be modified so that this legislation can be implemented on all of the Form MO-1040 returns. DOR estimates that it will take 4 programmers, 2 months to do this modification or 1,384 hours at a cost of \$46,170.

Customer Assistance anticipates numerous telephone calls and walk-ins in the Tax Assistance Centers. One Tax Collection Tech will be needed for every 15,000 calls a year to 751-7200 regarding balance dues on a denied subtraction due to failure to provide documentation to support exemption. DOR assumes 1 Tax Collection Tech will be needed for every 24,000 calls a year to 751-3505 hotline regarding the exemption, 1 Tax Processing Tech for every 5,200 additional telephone calls or 2,150 walk-ins in the Tax Assistance Centers.

DOR will have to modify the Form W-4 to allow for the new exempt status for the graduate.

Oversight assumes since less than nine thousand graduates are estimated to qualify for this exemption in FY06 (less than eighteen thousand in FY07), DOR can handle the increased workload from this legislation with the addition of one Tax Processing Technician I.

Oversight has, for fiscal note purposes only, changed the starting salary for the Tax Processing Tech I to correspond to the second step above minimum for comparable positions in the state's merit system pay grid. This decision reflects a study of actual starting salaries for new state employees for a six month period and the policy of the Oversight Subcommittee of the Joint Committee on Legislative Research.

Officials from the **Office of Administration, Budget and Planning (BAP)** assume this legislation has no impact on BAP.

BAP assumes this proposal provides that for all tax years beginning January 1, 2005, new master's or doctoral graduates from a Missouri institution who become employed in Missouri shall be exempt from income tax. This proposal excludes medical doctors and lawyers.

ASSUMPTION (continued)

Data supplied by the Coordinating Board for Higher Education indicate that, on average, there are 14,000 master's degrees awarded by Missouri institutions each year. An estimated 60% of these graduates (8,400) stay in Missouri, and earn an average of \$39,000 annually. Similarly, on average 700 doctoral degrees that meet the above definition are earned in Missouri each year. An estimated 34% of these graduates stay in Missouri (238) and earn an average of \$51,000 annually. Taken together, the total salary earned by these graduates is \$339.7 million.

Assuming that each of these graduates is single with no dependents and no other income, the following calculations apply (in millions of dollars):

Federal adjusted gross income:	339.7	
Federal standard deduction (\$4,750):	41.0	
Missouri standard deduction (\$2,100):	18.1	
Missouri deduction for federal taxes: (equal to the number of graduates X \$5000)		43.2
Missouri adjusted gross income:	237.4	
Tax on income up to \$9000 (number of graduates X \$315):	2.7	
Marginal Income:	159.7	
Tax on Marginal Income (6%):	9.6	
Total negative general revenue impact:	12.3	

This proposal would be effective for tax year 2005; therefore the first year of impact would be fiscal year 2006. Further this proposal allows graduates to take this deduction for the first three years after degree completion. Thus, in fiscal year 2007, the impact would be a negative \$24.6 million, and in fiscal year 2008, a negative \$36.9 million. This proposal would lower total state revenue.

Officials from the **Coordinating Board of Higher Education** assume the total fiscal impact of this legislation is unknown. In FY02, 14,098 students graduated with graduate and doctoral degrees from Missouri public and private institutions. According to the U.S. Census Bureau in 2001, the median earnings for Missouri master degree holders was \$35,000 and \$44,000 for doctoral degree recipients.

This legislation will decrease Total State Revenue.

<u>FISCAL IMPACT - State Government</u>	FY 2005 (10 Mo.)	FY 2006	FY 2007
GENERAL REVENUE FUND			
<u>Loss - General Revenue</u>			
Exemption for certain graduates from state income tax	\$0	(\$12,300,000)	(\$24,600,000)
<u>Cost - Dept. of Revenue</u>			
Personal Service (1 FTE)	\$0	(\$20,336)	(\$20,844)
Fringe Benefits	\$0	(\$8,419)	(\$8,629)
Expense and Equipment	\$0	(\$6,173)	(\$315)
Programming	<u>\$0</u>	<u>(\$46,170)</u>	<u>0</u>
Total Costs - DOR	<u>\$0</u>	<u>(\$81,098)</u>	<u>(\$29,788)</u>
ESTIMATED NET EFFECT ON GENERAL REVENUE FUND	<u>\$0</u>	<u>(\$12,381,098)</u>	<u>(\$24,629,788)</u>

<u>FISCAL IMPACT - Local Government</u>	FY 2005 (10 Mo.)	FY 2006	FY 2007
	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>

FISCAL IMPACT - Small Business

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

DESCRIPTION

This proposal creates the Keeping Missouri's Brightest Act.

The proposal exempts from state income tax the first three years of income earned by any person who completes a masters or doctoral degree from any public or private university located in Missouri.

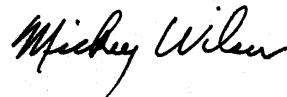
DESCRIPTION (continued)

The provisions of the bill will expire six years from the effective date.

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
Coordinating Board of Higher Education



Mickey Wilson, CPA
Director
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