

COMMITTEE ON LEGISLATIVE RESEARCH  
OVERSIGHT DIVISION

**FISCAL NOTE**

L.R. No.: 4148-01  
Bill No.: HB 1300  
Subject: Taxation and Revenue - Income  
Type: Original  
Date: February 23, 2004

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**FISCAL SUMMARY**

<b>ESTIMATED NET EFFECT ON GENERAL REVENUE FUND</b>			
FUND AFFECTED	FY 2005	FY 2006	FY 2007
General Revenue	\$0	(\$8,801,252)	(\$34,888,925)
<b>Total Estimated Net Effect on General Revenue Fund</b>	<b>\$0</b>	<b>(\$8,801,252)</b>	<b>(\$34,888,925)</b>

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

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

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

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

### FISCAL ANALYSIS

#### ASSUMPTION

Officials of the **Department of Revenue (DOR)** state this legislation phases in an earned income tax credit on the Missouri income tax return. For tax year beginning on January 1, 2006, a resident individual is authorized a state earned income tax credit equal to five percent of the Federal earned income tax credit. Beginning January 1, 2008, a taxpayer is authorized a state earned income tax credit equal to ten percent, and beginning January 1, 2010, a taxpayer is authorized a state earned income tax credit equal to twenty percent of the Federal earned income tax credit. If the credit exceeds the taxpayer's liability, the credit may be refunded or carried forward. DOR is required to notify any taxpayer who potentially may be eligible for the tax credit and who did not claim the credit on the state tax return.

According to the Federal Statistics of Income Bulletin used in Fiscal Note 3111-02 in the 2002 session, there are 379,333 federal returns filed by Missouri residents claiming an earned income tax credit. DOR assumes this credit will have an extra 20 second impact on all returns processed. The Division of Taxation will need two temporary tax season employee (\$7.50 an hour) for keying the additional line, one Tax Processing Technician for every 3,000 pieces of correspondence received regarding the credit, and one Tax Processing Technician for every 30,000 additional errors generated by this credit.

#### ASSUMPTION (continued)

DOR assumes Customer Assistance will need additional tax assistance field personnel to handle the walk-in questions until the credit is maximized. One Taxpayer Services Representative is requested for every additional 1,285 walk-ins per year. Also, the Customer Assistance Bureau anticipates the call volume to increase. A telephone collector can handle 2,000 calls per month, therefore, one Tax Collection Technician is requested for every 24,000 additional calls received regarding this credit.

DOR assumes this legislation will require modifications to the individual income tax systems. The Division of Taxation estimates these modifications, including programming changes, will require 1,384 hours of overtime at a cost of \$46,170. State Data Center charges will increase due to the additional storage and fields to be captured. Funding in the amount of \$3,657 is requested for implementation costs.

In a response to a prior similar proposal, DOR requested 5 Temporary Tax Season Employees to key and process the tax credits in order to maintain current processing times. DOR stated all other FTE needed will be requested through the normal budget process once the DOR has processed the credit and has numbers to determine the amount of errors and correspondence received, and the increase in telephone calls and walk-ins. DOR estimated the modifications to the individual income tax system, including programming changes, would require 1,125 hours of overtime at a cost of \$29,422. **Oversight** assumes DOR could handle this proposal with the same resources requested in the prior fiscal note (379,333 returns / 75,000 = 5 temps.) and will show costs for DOR for 5 temporary tax season employees, programming costs of \$46,170, and implementation costs of \$3,657.

Officials of the **Office of Administration, Budget and Planning (BAP)** assume this proposal creates a phased-in earned income tax credit (EIC), beginning with tax year 2006. Thus, this proposal would likely have no impact until FY 2007. There may be some impact in FY 2006 if workers that qualify for the EIC adjust their withholding downward in anticipation of this credit.

For tax year 2006, a resident allowed a federal EIC shall be allowed a credit against Missouri Adjusted Gross Income in an amount equal to 5% of the federal EIC. According to Statistics of Income Data – 2001 published by the IRS, \$631.3 million in credits were allowed in Missouri in tax year 2001.

The income ceiling for claiming the credit at the federal level is adjusted for inflation each year. Assuming 2% growth in the amount claimed for the credit each year, by 2006 an estimated \$697 million in earned income credits will be claimed in Missouri. Taken at 5%, this proposal would

ASSUMPTION (continued)

have a negative impact on general and total state revenues of \$34.85 million in FY 2007. BAP assumes this proposal would have no impact on their agency.

According to officials at the **University of Missouri, Research Center (UMRC)**, this bill creates a phased-in earned income tax credit for Missouri citizens. The tax credit is phased-in over three separate increments. The state credit is equal to 5% of the federal credit in 2006 and 2007, equal to 10% in 2008 and 2009, and equal to 20% in 2010 and 2011. This bill also provides for a sunset in 2012, six years after the effective date.

Because tax credits are modifications to taxes after the gross tax due is calculated, UMRC presents the impact the bill is expected to have on net tax revenues. UMRC estimates the implementation of this bill would reduce net taxes collected from individual income taxation by \$32.3 million in 2006 and 2007. In 2008 and 2009, net taxes collected would decline by \$64.6 million each year. Finally, in 2010 and 2011, the state earned income tax credit would reduce net taxes collected by \$129.2 million each year.

**Oversight** assumes DOR would require verification of eligibility. In the absence of such verification, total credits could be significantly greater than estimated.

**Oversight** will reflect the revenue impact for this proposal at the higher estimate of \$34.85 million for FY07 as calculated by BAP.

**Oversight** estimates a loss to the General Revenue Fund of \$8.7 million for FY06 due to the possibility of reduced withholding and estimated income tax payments for calendar year 2005. Oversight assumes 25% of Missouri taxpayers would adjust payments, however it should be noted that this amount could be less depending on the taxpayers' awareness of this credit in determining state income tax and their desire to adjust withholdings or estimated payments.

**This proposal would result in a decrease in Total State Revenues.**

FISCAL IMPACT - State Government

FY 2005  
(10 Mo.)

FY 2006

FY 2007

## GENERAL REVENUE FUND

### Loss to General Revenue Fund

Earned Income Tax Credit	\$0	(\$8,712,500)	(\$34,850,000)
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### Cost - Department of Revenue

Personal Service (5 Temps.)	\$0	(\$38,925)	(\$38,925)
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Programming	\$0	(\$49,827)	\$0
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Total Costs - DOR	\$0	(\$88,752)	(\$38,925)
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### ESTIMATED NET EFFECT ON GENERAL REVENUE FUND

	<u>\$0</u>	<u>(\$8,801,252)</u>	<u>(\$34,888,925)</u>
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### FISCAL IMPACT - Local Government

FY 2005  
(10 Mo.)

FY 2006

FY 2007

\$0

\$0

\$0

### FISCAL IMPACT - Small Business

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

### DESCRIPTION

This proposal allows a state individual income tax credit equal to a percentage of any earned income tax credit claimed by the taxpayer on the federal income tax return. The percentage of the federal credit allowed will be 5% for tax years 2006 and 2007, 10% for tax years 2008 and 2009, and 20% for tax year 2010 and thereafter. Any amount of credit which exceeds the taxpayer's liability in any tax year will be refunded to the taxpayer or carried forward into future tax years.

### DESCRIPTION (continued)

The bill also requires the Department of Revenue to notify potentially eligible taxpayers that they may be able to receive the earned income tax credit.

KS:LR:OD (12/02)

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  
University of Missouri Research Center  
Office of Administration  
Budget and Planning

A handwritten signature in black ink that reads "Mickey Wilson". The signature is written in a cursive, flowing style.

Mickey Wilson, CPA  
Director  
February 23, 2004