COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 4162-02
Bill No.: HCS for HB 1357
Subject: Tax Credits, Taxation and Revenue - Income, Department of Revenue
Type: Original
Date: January 31, 2018

Bill Summary: This proposal relates to income tax, with a contingent effective date for the earned income tax credit.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND				
FUND AFFECTED	FY 2019	FY 2020	FY 2021	Fully Implemented (FY 2028)
General Revenue	$0	(Could Exceed $7,300,000 to $49,657,000)	(Could Exceed $42,357,000 to $66,457,000)	(Could Exceed $97,900,000 to $140,257,000)
Total Estimated Net Effect on General Revenue	**$0**	**(Could Exceed $7,300,000 to $49,657,000)**	**(Could Exceed $42,357,000 to $66,457,000)**	**(Could Exceed $97,900,000 to $140,257,000)**

ESTIMATED NET EFFECT ON OTHER STATE FUNDS				
FUND AFFECTED	FY 2019	FY 2020	FY 2021	Fully Implemented (FY 2028)
Total Estimated Net Effect on Other State Funds	**$0**	**$0**	**$0**	**$0**

Numbers within parentheses: ( ) indicate costs or losses. This fiscal note contains 14 pages.

ESTIMATED NET EFFECT ON FEDERAL FUNDS				
FUND AFFECTED	FY 2019	FY 2020	FY 2021	Fully Implemented (FY 2028)
Total Estimated Net Effect on All Federal Funds	**$0**	**$0**	**$0**	**$0**

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)				
FUND AFFECTED	FY 2019	FY 2020	FY 2021	Fully Implemented (FY 2028)
Total Estimated Net Effect on FTE	**0**	**0**	**0**	**0**

☒ Estimated Net Effect (expenditures or reduced revenues) expected to exceed $100,000 in any of the three fiscal years after implementation of the act.

ESTIMATED NET EFFECT ON LOCAL FUNDS				
FUND AFFECTED	FY 2019	FY 2020	FY 2021	Fully Implemented (FY 2028)
Local Government	**$0**	**$0**	**$0**	**$0**

FISCAL ANALYSIS

ASSUMPTION

§135.760 Missouri Earned Income Tax Credit and §143.011 Individual Income Tax

Officials at the **University of Missouri's Economic and Policy Analysis Research Center** (**EPARC**) assume this bill would authorize an earned income tax credit in Missouri equal to 20% of filers' federal earned income credit. As well, this bill would increase the taxable income brackets as they pertain to the individual income tax. Starting in the year 2019, this bill would additionally increase the taxable income brackets by the amount of the growth in CPI in the year 1934. In 2020 it would additionally increase the taxable income brackets by the amount of the growth in CPI in the year 1935. In 2021 it would additionally increase the taxable income brackets by the amount of the growth in CPI in the year 1936. This process of an additional increase by the CPI of a corresponding historical tax year in the taxable income brackets would occur until the year 2100 where the 2015 increase in CPI would be added.

We will assume the inflation rate for the Missouri tax brackets for the future years 2019, 2020 and 2021 will increase by 1.38%, the latest available three-year annual average. The annual inflation increase in 1934 was 3.08%. The annual inflation increase in 1935 was 2.24%. The annual inflation increase in 1936 was 1.46%.

Baseline 2019

If the Missouri taxable income is:	The tax is:
Not over $1,042 …	1 ½ % of the Missouri taxable income
Over $1,042 but not over $2,084 …	$16 plus 2 % of excess over $1,042
Over $2,084 but not over $3,127 …	$36 plus 2 ½ % of excess over $2,084
Over $3,127 but not over $4,169 …	$63 plus 3 % of excess over $3,127
Over $4,169 but not over $5,211 …	$94 plus 3 ½ % of excess over $4,169
Over $5,211 but not over $6,253 …	$130 plus 4 % of excess over $5,211
Over $6,253 but not over $7,295 …	$172 plus 4 ½ % of excess over $6,253
Over $7,295 but not over $8,337 …	$219 plus 5 % of excess over $7,295
Over $8,337 but not over $9,381 …	$271 plus 5 ½ % of excess over $8,337
Over $9,381 …	$328 plus 5.9 % of excess over $9,381

Simulation 2019

If the Missouri taxable income is:	The tax is:
Not over $1,074 …	1 ½ % of the Missouri taxable income
Over $1,074 but not over $2,148 …	$16 plus 2 % of excess over $1,074
Over $2,148 but not over $3,222 …	$38 plus 2 ½ % of excess over $2,148

Over $3,222 but not over $4,295 …	$64 plus 3 % of excess over $3,222

ASSUMPTION (continued)

Over $4,295 but not over $5,369 …	$97 plus 3 ½ % of excess over $4,295
Over $5,369 but not over $6,443 …	$134 plus 4 % of excess over $5,369
Over $6,443 but not over $7,517 …	$177 plus 4 ½ % of excess over $6,443
Over $7,517 but not over $8,591 …	$226 plus 5 % of excess over $7,517
Over $8,591 but not over $9,666 …	$279 plus 5 ½ % of excess over $8,591
Over $9,666 …	$338 plus 5.9 % of excess over $9,666

The baseline for our analysis where Net Tax Due is $5,445.953 million where the taxable income brackets were increased by 1.38% from 2018 levels. The simulation results of the parameter changes in this bill for 2019 where the taxable income brackets were increased by an additional 3.08% and an earned income credit for Missourians is authorized shows Net Tax Due equals $5,388.610 million. This is a decrease in Net Tax Due of $57.343 million from the baseline. Therefore, this corresponds to a decrease in Net General Revenue in 2019 of $57.343 million due to this change in the Missouri tax brackets and rates.

Baseline 2020

If the Missouri taxable income is:	The tax is:
Not over $1,056 …	1 ½ % of the Missouri taxable income
Over $1,056 but not over $2,113 …	$16 plus 2 % of excess over $1,056
Over $2,113 but not over $3,170 …	$37 plus 2 ½ % of excess over $2,113
Over $3,170 but not over $4,227 …	$63 plus 3 % of excess over $3,170
Over $4,227 but not over $5,283 …	$95 plus 3 ½ % of excess over $4,227
Over $5,283 but not over $6,339 …	$132 plus 4 % of excess over $5,283
Over $6,339 but not over $7,396 …	$174 plus 4 ½ % of excess over $6,339
Over $7,396 but not over $8,452 …	$222 plus 5 % of excess over $7,396
Over $8,452 but not over $9,510 …	$275 plus 5 ½ % of excess over $8,452
Over $9,510 …	$333 plus 5.9 % of excess over $9,510

Simulation 2020

If the Missouri taxable income is:	The tax is:
Not over $1,113 …	1 ½ % of the Missouri taxable income
Over $1,113 but not over $2,226 …	$17 plus 2 % of excess over $1,113
Over $2,226 but not over $3,339 …	$39 plus 2 ½ % of excess over $2,226
Over $3,339 but not over $4,450 …	$67 plus 3 % of excess over $3,339
Over $4,450 but not over $5,563 …	$100 plus 3 ½ % of excess over $4,450
Over $5,563 but not over $6,676 …	$139 plus 4 % of excess over $5,563

Over $6,676 but not over $7,789 …	$184 plus 4 ½ % of excess over $6,676
Over $7,789 but not over $8,902 …	$234 plus 5 % of excess over $7,789

ASSUMPTION (continued)

Over $8,902 but not over $10,016 …	$289 plus 5 ½ % of excess over $8,902
Over $10,016 …	$351 plus 5.9 % of excess over $10,016

The baseline for our analysis where Net Tax Due is $5,439.853 million where the taxable income brackets were increased by 1.38% from 2019 levels. The simulation results of the parameter changes in this bill for 2020 where the taxable income brackets were increased by an additional 2.24% and an earned income credit for Missourians is authorized shows Net Tax Due equals $5,371.644 million. This is a decrease in Net Tax Due of $68.209 million from the baseline. Therefore, this corresponds to a decrease in Net General Revenue in 2020 of $68.209 million due to this change in the Missouri tax brackets and rates.

Baseline 2021

If the Missouri taxable income is:	The tax is:
Not over $1,071 …	1 ½ % of the Missouri taxable income
Over $1,071 but not over $2,142 …	$16 plus 2 % of excess over $1,071
Over $2,142 but not over $3,214 …	$37 plus 2 ½ % of excess over $2,142
Over $3,214 but not over $4,285 …	$64 plus 3 % of excess over $3,214
Over $4,285 but not over $5,356 …	$96 plus 3 ½ % of excess over $4,285
Over $5,356 but not over $6,426 …	$134 plus 4 % of excess over $5,356
Over $6,426 but not over $7,498 …	$177 plus 4 ½ % of excess over $6,426
Over $7,498 but not over $8,569 …	$225 plus 5 % of excess over $7,498
Over $8,569 but not over $9,641 …	$278 plus 5 ½ % of excess over $8,569
Over $9,641 …	$337 plus 5.9 % of excess over $9,641

Simulation 2021

If the Missouri taxable income is:	The tax is:
Not over $1,145 …	1 ½ % of the Missouri taxable income
Over $1,145 but not over $2,289 …	$17 plus 2 % of excess over $1,145
Over $2,289 but not over $3,434 …	$40 plus 2 ½ % of excess over $2,289
Over $3,434 but not over $4,576 …	$69 plus 3 % of excess over $3,434
Over $4,576 but not over $5,721 …	$103 plus 3 ½ % of excess over $4,576
Over $5,721 but not over $6,866 …	$143 plus 4 % of excess over $5,721
Over $6,866 but not over $8,010 …	$189 plus 4 ½ % of excess over $6,866
Over $8,010 but not over $9,155 …	$240 plus 5 % of excess over $8,010
Over $9,155 but not over $10,300 …	$298 plus 5 ½ % of excess over $9,155

Over $10,300 …	$361 plus 5.9 % of excess over $10,300

ASSUMPTION (continued)

The baseline for our analysis where Net Tax Due is $5,431.422 million where the taxable income brackets were increased by 1.38% from 2020 levels. The simulation results of the parameter changes in this bill for 2021 where the taxable income brackets were increased by an additional 1.46% and an earned income credit for Missourians is authorized shows Net Tax Due equals $5,356.772 million. This is a decrease in Net Tax Due of $74.650 million from the baseline. Therefore, this corresponds to a decrease in Net General Revenue in 2021 of $74.650 million due to this change in the Missouri tax brackets and rates.

Conclusion: If this bill were enacted we would expect Net General Revenue to decrease by $57.343 million in 2019, decrease by $68.209 million in 2020 and then decrease by $74.650 million in 2021 due to the portions of this bill that changes the Missouri individual income tax code.

§135.760 Missouri Earned Income Tax Credit

Officials at the **Office of Administration Division of Budget and Planning** (**B&P**) assume this proposal provides a non-refundable Earned Income Tax Credit to resident taxpayers in an amount equal to 20% of the federal EITC starting in tax year 2019, or upon growth in net General Revenue sufficient enough to trigger an income tax rate reduction, after accounting for the estimated loss from this section. For the purpose of this fiscal note, B&P will use a tax year 2019 start date for this section.

Using tax year 2015 data, the most recent year available, and accounting for the federal tax reform that took effect January 1, 2018; B&P estimates that a non-refundable earned income tax credit will reduce Total State Revenue and General Revenue by $34.1 million annually beginning in FY 2020.

Officials at the **Department of Revenue** (**DOR**) assume this proposal creates the Missouri Earned Income Tax Credit Act (EITC). Beginning January 1, 2019, the legislation allows eligible taxpayers a tax credit equal to twenty percent of the amount the taxpayer received under the federal earned income tax credit. If the credit exceeds the taxpayer's tax liability, the legislation prohibits refunding or carrying forward the credit to subsequent tax years.

The legislation requires the Department to prepare an annual report consisting of the amount of revenue expended on the earned income tax credit, the number of credits claimed, and the average value of the credit issued. In addition, the Department is required to contract with nonprofit groups in order to notify taxpayers of their potential eligibility to receive the credit.

ASSUMPTION (continued)

DOR estimates that a non-refundable earned income tax credit will reduce Total State Revenue and General Revenue by $61.8 million annually beginning in FY 2019.

DOR assumes the Personal Tax Section will require one Temporary Tax Employee ($89,164) and one Revenue Processing Technician I ($26,340) for every 14,800 errors generated and one Revenue Processing Technician I ($26,340) for every 5,800 additional correspondence generated. The Collections & Tax Assistance Section anticipates increased calls to the non-delinquent tax line due to confusing this credit with the federal credit. The federal credit is refundable while this one is not. It is likely the taxpayer will miscalculate the percentage or fail to include a copy of the federal return creating adjustment notices. The section requires one Tax Collection Technician I ($26,340) for every 15,000 contact annually on the non-delinquent tax line. This individual requires CARES equipment and license.

DOR estimated the FTE costs as $145,970 in FY 2019, $146,397 in FY 2020 and $147,570 in FY 2021. DOR assumes it will be able to absorb the above listed costs. If multiple bills pass which require Department resources and updates, the Department could request additional FTE and related equipment and expenses through the appropriation process.

Oversight notes that in similar legislation creating the Missouri Earned Income Tax Credit this year, SB 939, EPARC estimated the following impact:

The individual income tax for Missouri (2016) is the baseline for the analysis. This baseline takes into account the Federal Tax Cuts and Jobs Act. Net Tax Due equals $5,454,004. If the aforementioned tax credit is implemented, Net Tax Due reduces to $5,411,647. This translates into a decrease in Net General Revenue of $42.357 million.

Note: The increase seen in the General Tax Credits figure is the complete measure of 20% of Missouri filers' Federal Earned Income Credit. Many filers are able to reduce their tax burden to zero before using their entire credit. Because this tax credit does not allow the remainder to be refunded to the filer, our impact estimation is only concerned with the reduction in Net Tax Due. To reiterate, our estimate is this bill will reduce Net General Revenue by $42.357 million.

Oversight notes that in prior fiscal notes this year, regarding the Earned Income Tax Credit, EPARC estimated an impact of $57 million. However, they have been able to recalculate the costs based on the Federal tax law changes.

Oversight notes that DOR estimates the EITC changes at $61.8 million, BAP estimates it at $34.1 million and EPARC estimates it at $42.357 million. DOR is not able to include the

Federal law changes that may impact future taxpayer filings in their calculation, while B&P and EPARC were able to include them. Oversight will show the impact of the EITC as "Could exceed" the estimate provided by EPARC.

Oversight notes this proposal in Section B states that this portion of the proposal would not become effective unless the growth in net General Revenue would be sufficient to trigger the reduction of the individual income tax under subsection 2 of §143.011. Oversight will show the impact of this proposal as $0 (trigger not met) or the estimate provided by EPARC.

§143.011 Individual Income Tax
Officials at the **B&P** assume this section would adjust the individual income tax brackets for inflation occurring from 1934 through 2015 starting on January 1, 2019. The first adjustment, for tax year 2018, is to reflect the rate of inflation in 1934. Each adjustment thereafter shall reflect the rate of inflation for the tax year 84 years prior. If there was no inflation during the historical tax year, DOR is to resume adjustments for historical inflation in the following year. Inflation adjustments are to continue until total adjustments equal 17.7%.

This proposal will automatically sunset two years after effective date unless re-authorized by the General Assembly. For the purpose of this fiscal note, B&P will estimate the full impact of this proposal as if it were re-authorized.

Based on data provided by the United States Census Bureau, B&P estimates that inflation adjustments would occur for the historical tax years of 1934 through 1942 which would correspond to tax years 2019 through 2027. B&P notes that there was no inflation during 1938 and 1939. B&P further notes that while inflation in 1942 was equal to 10.9%, B&P only adjusted the individual income tax brackets by 1.1%, because the cumulative adjustment cap of 17.7% had been met.

ASSUMPTION (continued)

Table 1 shows the inflation adjustment and loss to General Revenue by tax year.

Tax Year	Inflation Adjustment	Loss to GR (in millions)
2019	3.5%	16.2
2020	2.6%	29.8
2021	1.0%	35.7
2022	3.7%	51.0
2023	0.0%	54.8
2024	0.0%	55.4
2025	0.7%	60.7
2026	5.1%	88.3
2027*	1.1%	96.7

*The HB 1357 inflation adjustment is 1.1%, so that the cumulative adjustment totals 17.7%. However, inflation in that year was 10.9%.

Table 2 shows the inflation adjustment by fiscal year and the estimated loss to General Revenue.

Fiscal Year	Loss to GR (millions)
2019	6.8
2020	21.9
2021	32.3
2022	42.1
2023	52.6
2024	55.1
2025	57.6
2026	62.6
2027	91.8
2028	96.7

Using tax year 2015 data, the most current year available, B&P estimates that this section will reduce Total State Revenue and General Revenue in FY 2019 by $6.8 million and once fully implemented in FY 2028 it will reduce Total State Revenue and General Revenue by $96.7 million annually.

ASSUMPTION (continued)

Officials at the **DOR** assume this proposed section on January 1 2019, adjusts the amounts of Missouri taxable income listed in subsection 1 of this section by a percentage equal to the inflation rate that occurred in 1934. For each subsequent tax year, the director shall positively adjust the amounts of the Missouri taxable income by a rate equal to the amount of inflation during the corresponding historical year.

Tax Year	Inflation Adjustment	Reference Year
2019	3.5%	1934
2020	2.6%	1935
2021	1.0%	1936
2022	3.7%	1937
2023	0.0%	1938
2024	0.0%	1939
2025	0.7%	1940
2026	5.1%	1941
2027*	1.1%	1942

*The HCS HB 1357 inflation adjustment is 1.1%, so that the cumulative adjustment totals 17.7%. However, inflation in that year (1942) was 10.9%.

	Bracket Change Impact		
FY 2019	FY 2020	FY 2021	FY 2028
($7.3)	($24.1)	($34.4)	($97.9)

Figures in Millions

Oversight notes that DOR and B&P used the historical inflation rate to calculate the impact as required by the proposal, while EPARC used an average of 1.38% inflation rate. Oversight will show the impact of the bracket changes as “Could exceed” the estimate provided by DOR.

ASSUMPTION (continued)

Summary of Bill
Therefore, **B&P** estimates that this proposal will reduce Total State Revenue and General Revenue by $6.8 million in FY 2019 and $130.8 million in FY 2028, and annually thereafter, once fully implemented.

Fiscal Year	Loss to GR
2019	6.8
2020	56.0
2021	66.4
2022	76.2
2023	86.7
2024	89.2
2025	91.7
2026	96.7
2027	125.9
2028	130.8

figures in $M

Bill as a Whole
Oversight notes this proposal would be effective beginning January 1, 2019, which would have a fiscal impact to the state beginning in January 2020 when individual income tax returns would be filed. Oversight is aware that some taxpayers would adjust withholding or estimated tax payments in anticipation of a tax reduction, but for convenience and clarity will include the full impact for the tax year in the year tax returns would be filed.

Oversight also notes this proposal has a provision which would make the individual income tax bracket changing program sunset two years after its effective date; in this case the program would sunset December 31, 2020 and would have no additional impact after that date unless the program is re-authorized. Oversight notes that this proposal, if renewed, would reach its full impact in FY 2028. Oversight will show the impact as if it is renewed until its fully impacted year of FY 2028.

Officials at the **Joint Committee on Administrative Rules** assume there is no fiscal impact from this proposal.

Officials from the **Office of the Secretary of State (SOS)** state many bills considered by the General Assembly include provisions allowing or requiring agencies to submit rules and

ASSUMPTION (continued)

regulations to implement the act. The SOS is provided with core funding to handle a certain amount of normal activity resulting from each year's legislative session. The fiscal impact for this fiscal note to the SOS for Administrative Rules is less than $2,500. The SOS recognizes that this is a small amount and does not expect that additional funding would be required to meet these costs. However, the SOS also recognizes that many such bills may be passed by the General Assembly in a given year and that collectively the costs may be in excess of what the office can sustain with the core budget. Therefore, the SOS reserves the right to request funding for the cost of supporting administrative rules requirements should the need arise based on a review of the finally approved bills signed by the governor.

Oversight assumes the SOS could absorb the costs of printing and distributing regulations related to this proposal. If multiple bills pass which require the printing and distribution of regulations at substantial costs, the SOS could request funding through the appropriation process.

FISCAL IMPACT - State Government	FY 2019 (10 Mo.)	FY 2020	FY 2021	Fully Implemented (FY 2028)
GENERAL REVENUE				
Revenue Reduction - creation of the Missouri Earned Income Tax Credit §135.760	$0	$0 or (Could Exceed $42,357,000)	$0 or (Could Exceed $42,357,000)	$0 or (Could Exceed $42,357,000)
Revenue Reduction - changing the individual income brackets based on the historical inflation rates §143.011	$0	(Could Exceed $7,300,000)	(Could Exceed $24,100,000)	(Could Exceed $97,900,000)
ESTIMATED NET EFFECT ON GENERAL REVENUE	**$0**	**(Could Exceed $7,300,000 to $49,657,000)**	**(Could Exceed $24,100,000 to $66,457,000)**	**(Could Exceed $97,900,000 to $140,257,000)**

FISCAL IMPACT - Local Government	FY 2019 (10 Mo.)	FY 2020	FY 2021	Fully Implemented (FY 2028)
	$0	**$0**	**$0**	**$0**

FISCAL IMPACT - Small Business

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

FISCAL DESCRIPTION

This bill establishes the "Missouri Earned Income Tax Credit Act" which authorizes an individual income tax credit equal to 20% of any earned income tax credit claimed by the taxpayer on his or her federal income tax return, beginning on January 1, 2019. Any credit that exceeds the taxpayer's liability in any tax year cannot be refunded to the taxpayer. The Department of Revenue must notify taxpayers who may qualify for the credit and must contract with one or more nonprofit groups to contact non-English speaking individuals, elderly residents, tenants, and very low-income individuals who do not file tax returns to notify them annually of the credit. The department must prepare an annual report containing the number of credits issued and claimed, the total amount of revenue expended, and the average value of the credits issued within certain income ranges.

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
Joint Committee on Administrative Rules
Office of the Secretary of State
University of Missouri's Economic and Policy Analysis Research Center

Ross Strope

Acting Director
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