

COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 2454H.02I
Bill No.: HB 1202
Subject: Economic Development; Revenue, Department Of; Taxation And Revenue -
Income; Business And Commerce; Economic Development, Department Of;
Treasurer, State; Banks And Financial Institutions; Contracts And Contractors;
Consumer Protection
Type: Original
Date: March 3, 2021

Bill Summary: Changes the laws regarding linked deposits, home-based businesses,
taxation, non-compete agreements, and the Department of Economic
Development.

FISCAL SUMMARY

| ESTIMATED NET EFFECT ON GENERAL REVENUE FUND | | | | |
|--|--|--|--|--|
| FUND AFFECTED | FY 2022 | FY 2023 | FY 2024 | Fully Implemented (FY 2027) |
| General Revenue Fund | Less than or greater than (\$115,177,789) | Less than or greater than (\$399,763,362) | Less than or greater than (\$691,689,723) | Less than or greater than (\$1,024,272,200) |
| Total Estimated Net Effect on General Revenue | Less than or greater than (\$115,177,789) | Less than or greater than (\$399,763,362) | Less than or greater than (\$691,689,723) | Less than or greater than (\$1,024,272,200) |

| ESTIMATED NET EFFECT ON OTHER STATE FUNDS | | | | |
|---|---|---|---|---|
| FUND AFFECTED | FY 2022 | FY 2023 | FY 2024 | Fully Implemented (FY 2027) |
| Other State Funds | Less than or greater than (\$77,411) | Less than or greater than (\$77,411) | Less than or greater than (\$77,411) | Less than or greater than (\$77,411) |
| | | | | |
| Total Estimated Net Effect on <u>Other</u> State Funds | Less than or greater than (\$77,411) | Less than or greater than (\$77,411) | Less than or greater than (\$77,411) | Less than or greater than (\$77,411) |

Numbers within parentheses: () indicate costs or losses.

| ESTIMATED NET EFFECT ON FEDERAL FUNDS | | | | |
|---|------------|------------|------------|-----------------------------|
| FUND AFFECTED | FY 2022 | FY 2023 | FY 2024 | Fully Implemented (FY 2027) |
| | | | | |
| | | | | |
| 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 2022 | FY 2023 | FY 2024 | Fully Implemented (FY 2027) |
| General Revenue – DOR | 3 FTE | 3 FTE | 3 FTE | 3 FTE |
| | | | | |
| Total Estimated Net Effect on FTE | 3 FTE | 3 FTE | 3 FTE | 3 FTE |

☒ 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 2022 | FY 2023 | FY 2024 | Fully Implemented (FY 2027) |
| | | | | |
| Local Government | \$0 | \$0 | \$0 | \$0 |

FISCAL ANALYSIS

ASSUMPTION

Officials from the **Office of Administration – Budget & Planning Division (B&P)** state this proposed legislation will decrease Total State Revenue (TSR) by \$1,023,996,400 once fully implemented.

B&P states this proposed legislation will impact the calculation under Article X, Section 18(e).

Section 30.750 – Linked Deposits, Farm Assistance, Small Business and Water Systems Loans

Officials from **B&P** state this section would expand the definition of “eligible small business” for the purpose of linked deposit accounts. B&P notes that the maximum deposits that may be made by the Treasurer into such accounts is in Section 30.753, which is not changed in this proposal. Therefore, B&P estimates that this provision will not have an impact.

Officials from the **Missouri Department of Revenue (DOR)** do not anticipate this section will result on a fiscal impact on their organization. Oversight does not have any information to the contrary. Therefore, Oversight will not report a fiscal impact for this organization as it relates to this section.

Oversight notes this section modifies the definition of “Eligible Small Business”.

The definition of Eligible Small Business is expanded to include “a person who receives a loan from the Small Business Administration; however, a person eligible under this paragraph shall not receive a linked deposit in an amount more than ten percent (10%) of the amount of the loan from the Small Business Administration or two hundred fifty thousand dollars (\$250,000), whichever is less, and, if such person relocates out of this state within ten (10) years of receiving the linked deposit, the person shall be required to repay the interest forgone on the linked deposit rate to the state”.

Oversight notes the Missouri Linked Deposits Program (Missouri FIRST) is a statutorily created lending program managed by the Missouri State Treasurer. Missouri FIRST is aimed to expand and strengthen Missouri’s communities by working with Missouri’s financial institutions to provide low-interest loans to qualified borrowers for business growth and development.

Per the [Missouri FIRST Linked Deposit Program 2020 Annual Report](#), Missouri FIRST placed 1,085 loans in the 2020 program year totaling \$437,486,163.

Oversight notes eligible borrowers/loan programs include:

- Small businesses with up to 99 employees
- Agriculture
- Multi-Family Housing
- Job Enhancement
- Local governments
- Alternative-energy focused programs

Oversight assumes the modification(s) to this section are specific to the Small Business Program under Missouri FIRST.

Oversight notes, per the Missouri FIRST Linked Deposit Program 2020 Annual Report, the following total loan amounts have been issued under the Small Business Program:

| Missouri FIRST | | | | | | | |
|--|---------------|---------------|---------------|---------------|---------------|---------------|---------------|
| Program Year | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
| Total Loan Amounts - Small Business Program | \$257,414,575 | \$213,070,643 | \$171,373,606 | \$159,921,379 | \$238,027,410 | \$274,786,750 | \$209,752,941 |

Oversight notes, per Section 30.753, no more than one hundred ninety million dollars (\$190,000,000) of the aggregate deposit (\$800,000,000) shall be used for linked deposits to small businesses. However, Per Section 30.753, if demand for a particular type of linked deposit exceeds the initial allocation, and funds initially allocated to another type are available and not in demand, the Missouri State Treasurer may commingle allocations among the types of linked deposits.

Based on the information shown above, in regards to the total loan amounts for the Small Business Program, in conjunction with the “cap” established for the Small Business Program equal to one hundred ninety million dollars (\$190,000,000), demand for the Small Business type of linked deposits is high.

Based on the Missouri FIRST Linked Deposit Program 2020 Annual Report, the Small Business Program accounted for the largest portion of active loans. The chart below reports the Small Business Program as a percentage of total active loan(s):

| |
|---|
| Missouri FIRST - Small Business Program |
|---|

| Program Year | 2018 | 2019 | 2020 |
|--------------|------|------|------|
| Percent | 61% | 53% | 43% |

During the 2020 program year, Missouri FIRST issued 196 **new loans** totaling \$59,800,102. Of the \$59,800,120 issued in loans during the 2020 program year, \$32,942,975 was issued under the Small Business Program.

Oversight notes, then, the Small Business Program received approximately fifty five percent (55%) of the total amount of loans issued during program year 2020 (\$32,942,975 / \$59,800,102).

Assuming the number of new loans issued during the 2020 program year, under the Small Business Program, totaled fifty five percent (55%) of the total, Oversight estimates approximately 108 **new** loans ($196 * 55\%$) were issued under the Small Business Program during the 2020 program year.

Therefore, Oversight estimates the average amount received for **each** “new” eligible small business totals \$305,028 ($\$32,942,975 / 108$).

Oversight notes this section would cap the amount a newly eligible small business would be able to receive at two hundred fifty thousand dollars (\$250,000).

Oversight notes, in response to legislation that increased the aggregate amount of deposit (TAFP HCS for SCS for SB 599 – 2020), the Missouri State Treasurer’s Office indicated the opportunity cost was approximately 2.207%.

Therefore, Oversight assumes, should one **new** small business that becomes eligible under this proposed legislation receive a loan in the amount of 250,000, the potential impact would be:

$$((\$32,942,975 + \$250,000) - \$32,942,975) * 2.207\% \text{ or } \$250,000 * 2.207\% = \$5,518$$

In response to TAFP HCS for SCS for SB 599 (2020), the Missouri State Treasurer’s Office indicated the impact to General Revenue (GR) is equal to 39% of the total impact and the impact to “Other State Funds” is equal to 61% of the total impact.

Therefore, Oversight estimates, for each **new** loan to a newly eligible small business, GR would be reduced by \$2,152 ($\$5,518 * 39\%$) and “Other State Funds” would be reduced by \$3,366 ($\$5,518 * 61\%$).

Oversight restates that the definition of Eligible Small Business is expanded to include “a person who receives a loan from the Small Business Administration; however, a person eligible under this paragraph shall not receive a linked deposit in an amount more than ten percent (10%) of the amount of the loan from the Small Business Administration or two hundred fifty thousand

dollars (\$250,000), whichever is less, and, if such person relocates out of this state within ten (10) years of receiving the linked deposit, the person shall be required to repay the interest forgone on the linked deposit rate to the state”.

Oversight notes, per the [U.S. Small Business Administration](#), approximately 23 Missouri businesses received financings under the Small Business Investment Company Program during Fiscal Year 2018. Oversight notes the total amount of financing totaled \$108,900,000. Therefore, Oversight assumes the average amount financed per business totals \$4,734,783 (\$108,900,000 / 23). Oversight notes ten percent (10%) of the average amount financed per business totals \$473,478. This is greater than the cap put forth for the newly eligible small businesses equal to \$250,000.

Therefore, Oversight estimates the total amount of linked deposit that would be permitted for the aforementioned small businesses would total 5,750,000 (\$250,000 * 23).

Using the equation previously used to determine what the impact would be should one small business qualify under the newly expanded definition of Eligible Small Business, Oversight estimates the impact should 23 small businesses qualify under the newly expanded definition of Eligible Small Business.

$((\$32,942,975 + \$5,750,000) - \$32,942,975) * 2.207\%$ **or** $\$5,750,000 * 2.207\%$ **or** $\$5,518 * 23 = \$126,903$

Therefore, **Oversight** estimates, should the 23 small businesses that received a loan from the Small Business Administration during Fiscal Year 2018 qualify under the newly expanded definition of Eligible Small Business and receive linked deposit, GR would be reduced by \$49,492 (\$126,902 * 39%) and “Other State Funds” would be reduced by \$77,411 (\$126,902 * 61%).

Oversight assumes the expanded definition of Eligible Small Business would become effective August 28, 2021 (Fiscal Year 2022).

Therefore, Oversight will report a revenue reduction to GR equal to an amount “Less than or greater than” \$49,492 and a revenue reduction to “Other State Funds” equal to an amount “Less than or greater than” \$77,441 beginning in Fiscal Year 2022 as a result of a **potential increase in participation in the Missouri FIRST Program as a result of expanding who qualifies.**

Oversight notes the reduction to revenues is the result of the lost opportunity for higher returns should investment have otherwise occurred elsewhere that provided larger returns.

Section 34.195 – State Contracts

Officials from **B&P** state this section would require that 5% of state contracts be awarded to businesses in operation for less than five (5) years.

Officials from the **DOR** do not anticipate this section will result on a fiscal impact on their organization. Oversight does not have any information to the contrary. Therefore, Oversight will not report a fiscal impact for this organization as it relates to this section.

Oversight notes this section states that five percent (5%) of all state contracts shall be awarded to businesses that have been in operation for less than five (5) years.

Oversight assumes a Request for Proposal would continue to be issued for many projects, in which the best suited business would be awarded the contract. Therefore, Oversight will assume any impact(s) as a result of this section would be indirect and Oversight will not report a fiscal impact for this section.

Section 143.073 and 143.513– Right To Start Act

Officials from **B&P** state **Section 143.073** would allow businesses who begin operations after August 28, 2021 to calculate their income taxes under this new section in lieu of the calculations under Sections 143.011, 143.021, and 143.071, RSMo. B&P notes that Section 143.011 contains the tax rate and brackets for Individual Income Tax, while Section 143.071 contains the tax rate for corporate income tax.

Subsection 143.073.2 would allow any corporation or other business entity, with a valid license, to utilize the income tax brackets and rates established under subdivision 3. B&P notes that this would include C-corporations, S-corporations, Sole Proprietorships, Partnerships, and Limited Liability Companies (LLCs).

Subsection 143.073.3 creates tax brackets and tax rates for qualifying businesses. Table 1 shows the income brackets and tax rates by tax year.

Table 1: Income Thresholds for Taxation

| Years of Operation | Lower Income | Tax Rate | Higher Income | Tax Rate |
|--------------------|--------------|----------|---------------|----------|
| 1 | \$250,000 | 0.0% | \$250,001 | 4.0% |
| 2 | \$500,000 | 1.0% | \$500,001 | 4.0% |
| 3 | \$750,000 | 2.0% | \$750,001 | 4.0% |
| 4 | \$1,000,000 | 3.0% | \$1,000,001 | 4.0% |
| 5 | all income | | | 4.0% |

Based on the 2017 Annual Business Survey (the most complete year available) published by the U.S. Census Bureau there were 18,032 firms in business for less than two (2) years in Missouri,

15,104 firms in business for 2 to 3 years, and 10,637 firms in business for four (4) to five (5) years. Table 2 shows the number of firms by length of operations.

Table 2: Business in Missouri

| Years of Operation | Number of firms | Average Annual Revenue |
|--------------------|-----------------|------------------------|
| < 2 | 18,032 | \$520,550 |
| 2 to 3 | 15,104 | \$639,351 |
| 4 to 5 | 10,637 | \$1,013,027 |
| 6 to 10 | 16,808 | \$1,341,666 |
| 11 to 15 | 16,568 | \$1,864,366 |
| > 15 | 39,007 | \$15,337,429 |

Based on information published by the National Small Business Association, approximately 35% of small businesses are LLCs, 33% are S-Corporations, 19% are C-Corporations, 12% are Sole Proprietorships, and 2% are Partnerships. Table 3 shows the estimated number of firms for each formation type.

Table 3: Estimated Businesses by Formation

| Years of Operation | Number of firms | LLC (35%) | S-Corp (33%) | C-Corp (19%) | Sole Proprietor (12%) | Partnerships (2%) |
|--------------------|-----------------|-----------|--------------|--------------|-----------------------|-------------------|
| < 2 | 18,032 | 6,275 | 5,914 | 3,390 | 2,128 | 325 |
| 2 to 3 | 15,104 | 5,256 | 4,954 | 2,840 | 1,782 | 272 |
| 4 to 5 | 10,637 | 3,702 | 3,489 | 2,000 | 1,255 | 191 |
| 6 to 10 | 16,808 | 5,849 | 5,513 | 3,160 | 1,983 | 303 |
| 11 to 15 | 16,568 | 5,766 | 5,434 | 3,115 | 1,955 | 298 |
| > 15 | 39,007 | 13,574 | 12,794 | 7,333 | 4,603 | 702 |
| Total | 116,156 | 40,422 | 38,098 | 21,838 | 13,706 | 2,091 |

Corporate Income Tax

B&P notes that as of January 1, 2020 the corporate tax rate under Section 143.071, RSMo. is 4.0%. Using the information above, B&P estimates that this provision will reduce an individual

firm's income tax by \$10,000 to \$15,000 per year in the first four years of operation. Table 4 shows the estimated impact per firm.

Table 4: Corporate Income Tax Impacts

| Year of Operation | Number of Businesses | Current Estimated Taxes | Proposed Estimated Taxes | Difference in Taxes Owed |
|-------------------|----------------------|-------------------------|--------------------------|--------------------------|
| 1 | 3,390 | \$20,822 | \$10,822 | (\$10,000) |
| 2 | 2,840 | \$25,574 | \$10,574 | (\$15,000) |
| 3 | 2,840 | \$25,574 | \$10,574 | (\$15,000) |
| 4 | 2,000 | \$40,521 | \$30,521 | (\$10,000) |
| 5 | 2,000 | \$40,521 | \$40,521 | \$0 |

To account for the number of business closures within the first five (5) years of operation, B&P utilized the number of firms operating less than 2 years, between 2 and 3 years, and between 4 and 5 years. B&P estimates that in total, this provision will reduce Corporate Income Taxes by \$139.1 million annually by Tax Year 2025. Table 5 shows the estimated impact by tax year.

Table 5: Corporate
Income Tax Loss by Tax
Year

| Tax Year | GR Loss |
|----------|-----------------|
| 2022 | (\$33,900,000) |
| 2023 | (\$76,500,000) |
| 2024 | (\$119,100,000) |
| 2025 | (\$139,100,000) |
| 2026 | (\$139,100,000) |

However, because this proposed legislation would begin at the beginning of a firm's tax year, the corporations will adjust their declarations payments during the first fiscal year. Based on historical revenue receipts, B&P estimates that 50% of corporate income taxes are remitted during Fiscal Year 1 and 50% are remitted during Fiscal Year 2. Therefore, B&P estimates that this provision will reduce TSR and General Revenue (GR) by \$17.0 million in Fiscal Year 2022. Once fully implemented in Fiscal Year 2027, this proposed legislation will reduce TSR and GR by \$139.1 million annually. Table 6 shows the estimated impact by fiscal year.

Table 6: Corporate
Income Tax Loss by
Fiscal Year

| Fiscal Year | GR Loss |
|-------------|-----------------|
| 2022 | (\$16,950,000) |
| 2023 | (\$55,200,000) |
| 2024 | (\$97,800,000) |
| 2025 | (\$129,100,000) |
| 2026 | (\$139,100,000) |
| 2027 | (\$139,100,000) |

Individual Income Tax

B&P notes that LLCs, S-Corporations, Sole Proprietorships, and Partnerships are all “pass-through” entities. Owners of such firms report business income on their Individual Income Tax form and not on a Corporate Income Tax form. B&P further notes that the Individual Income Tax rate is currently 5.4%, with three (3) additional 0.1% reductions scheduled to occur pending growth in net GR.

In addition, Section 143.022, RSMo. grants pass-through businesses and income exemption on a portion of their business income. B&P notes that currently 10% of pass-through business income is exempt from taxation, with two more 5% increases scheduled to occur pending net GR growth. B&P assumes that such pass-through businesses will still be able to claim the income exemption since Subsection 143.073.4 does not reference Section 143.022, RSMo. in the “in lieu of” references.

Based on current revenue forecasts and average revenue growth, B&P estimates that revenues in Fiscal Year 2021, Fiscal Year 2024, and Fiscal Year 2025 will reach the SB 509 (2014) growth trigger requirement for reductions to the top rate of tax and increased business exemption.

Therefore, the top rate of tax will be reduced by 0.1% in Tax Year(s) 2022, 2025, and 2026 and the business income exemption will increase by 5% in Tax Year(s) 2022 and 2025 under SB 509 (2014).

Accounting for changes scheduled to occur; B&P estimates that this provision will reduce per firm taxes owed by \$8,914 to \$15,752 per year for businesses started in Tax Year 2022. B&P

notes that businesses started in future years would face a different income tax structure due to the rate reduction and income exemption increase scheduled to occur under SB 509 (2014). Table 7 shows the estimated impact for firms established in Tax Year 2022.

Table 7: Pass-Through Income Tax Impacts for Businesses
Started in Tax Year 2022*

| Year of Operation | Number of Businesses | Current Estimated Taxes** | Proposed Estimated Taxes*** | Difference in Taxes Owed |
|-------------------|----------------------|---------------------------|-----------------------------|--------------------------|
| 1 | 14,642 | \$23,451 | \$7,699 | (\$15,752) |
| 2 | 12,264 | \$28,803 | \$6,738 | (\$22,065) |
| 3 | 12,264 | \$28,803 | \$10,869 | (\$17,934) |
| 4 | 8,637 | \$42,142 | \$24,313 | (\$17,829) |
| 5 | 8,637 | \$41,331 | \$32,417 | (\$8,914) |

*This is only the tax structure for businesses started in 2022.

**The estimates for current taxes accounts for the top rate reductions and business income exemptions under SB 509 (2014).

***The estimates for proposed taxes accounts for the business income exemptions under SB 509 (2014).

To account for the number of business closures within the first five (5) years of operation, B&P utilized the number of firms operating less than 2 years, between 2 and 3 years, and between 4 and 5 years. B&P estimates that in total, this provision will reduce Individual Income Taxes by \$884.9 million annually by Tax Year 2026. Table 8 shows the estimated impact by tax year.

Table 8: Individual Income
Loss by Tax Year

| Tax Year | GR Loss |
|----------|-----------------|
| 2022* | (\$230,641,824) |
| 2023 | (\$501,244,825) |
| 2024 | (\$721,184,752) |
| 2025* | (\$833,544,841) |
| 2026* | (\$884,896,400) |

*Assumes that SB 509 (2014) rate reduction and

business income
 exemption increase occurs

However, because this proposed legislation would begin at the beginning of a firm's tax year, individuals will adjust their withholdings and declarations during the first fiscal year. Based on historic revenue patterns, 42% of individual income taxes are remitted during Fiscal Year 1 and 58% are remitted during in Fiscal Year 2. Therefore, B&P estimates that this provision will reduce TSR and GR by \$96.9 million in Fiscal Year 2022. Once fully implemented in Fiscal Year 2027, this proposal will reduce TSR and GR by \$88.4 million annually. Table 6 shows the estimated impact by fiscal year.

Table 9: Individual Income
 Loss by Tax Year

| Fiscal Year | GR Loss |
|-------------|-----------------|
| 2022 | (\$96,869,566) |
| 2023 | (\$344,295,084) |
| 2024 | (\$593,619,595) |
| 2025 | (\$768,375,989) |
| 2026 | (\$855,112,496) |
| 2027 | (\$884,896,400) |

Summary

B&P estimates that this provision will reduce TSR and GR by \$113.8 million in Fiscal Year 2022. Once fully implemented, in Fiscal Year 2027 this provision will reduce TSR and GR by \$1.0 billion annually. Table 10 shows the estimated impact by fiscal year.

Table 10: Summary of GR
 Impact

| Fiscal Year | GR Loss |
|-------------|-------------------|
| 2022 | (\$113,819,566) |
| 2023 | (\$399,495,084) |
| 2024 | (\$691,419,595) |
| 2025 | (\$897,475,989) |
| 2026 | (\$994,212,496) |
| 2027 | (\$1,023,996,400) |

Officials from **DOR** state, starting January 1, 2022, this proposed legislation changes the corporate income tax rate currently at 4% to the following for eligible new businesses.

Table 1: Income Thresholds for Taxation

| Years of Operation | Lower Income | Tax Rate | Higher Income | Tax Rate |
|--------------------|--------------|----------|---------------|----------|
| 1 | \$250,000 | 0.00% | \$250,001 | 4.00% |
| 2 | \$500,000 | 1.00% | \$500,001 | 4% |
| 3 | \$750,000 | 2% | \$750,001 | 4% |
| 4 | \$1,000,000 | 3% | \$1,000,001 | 4% |
| 5 | all income | | | 4% |

This new Corporate Income Tax rate is in lieu of any other income tax imposed under Sections 143.011 (Individual Income Tax rates), 143.021 (limits on tax) and 143.071 (corporate tax rate). It should be noted that this proposed legislation does not prevent the business entities from claiming the business income exemptions under Section 143.022.

The proposed legislation defines “eligible new businesses” as a corporation or other business entity that begins operations in this state on or after the effective date of this proposal. This would include C-Corps as well as entities that may currently file as pass through businesses using their Individual Income Tax return. These entities could now choose to file under the corporate tax rate which is less than the Individual Income Tax rate (5.3%). Such entities are LLC, S-Corps, Sole Proprietors, and Partnerships. It is estimated that businesses are currently distributed as follows:

Table 2: Formation of Small Businesses

| | |
|-----------------|-----|
| LLC | 35% |
| S-Corp | 33% |
| C-Corp | 19% |
| Sole Proprietor | 12% |
| Partnerships | 2% |

While some businesses may want to try to close and then reopen in order to take advantage of these reduced tax rates, should they use their same federal employment identification number and Missouri identification number DOR would consider their whole previous business history

in determining placement on the sliding tax rate scale. Additionally, DOR currently monitors the closing and reopening of businesses to avoid tax liability.

For the purposes of the calculations we assumed the following annual revenue per year.

Table 3: Business in Missouri

| Est. MO Business | Years of Operation | Average Annual Revenue |
|------------------|--------------------|------------------------|
| 18,032 | < 2 | \$520,550 |
| 15,104 | 2 to 3 | \$639,351 |
| 10,637 | 4 to 5 | \$1,013,027 |
| 16,808 | 6 to 10 | \$1,341,666 |
| 16,568 | 11 to 15 | \$1,864,366 |
| 39,007 | > 15 | \$15,337,429 |

The current tax rate for C-Corps is 4%. Using information on the number of new businesses that are created annually, we estimated the difference between the taxes expected to be paid under current law and the proposed law.

Table 4: Corporate Income Tax Impacts

| Year of Operation | Number of Businesses | Current Estimated Taxes | Proposed Estimated Taxes | Difference in Taxes Owed |
|-------------------|----------------------|-------------------------|--------------------------|--------------------------|
| 1 | 3,390 | \$20,822 | \$10,822 | (\$10,000) |
| 2 | 2,840 | \$25,574 | \$10,574 | (\$15,000) |
| 3 | 2,840 | \$25,574 | \$10,574 | (\$15,000) |
| 4 | 2,000 | \$40,521 | \$30,521 | (\$10,000) |
| 5 | 2,000 | \$40,521 | \$40,521 | \$0 |

Which would result in a loss to general revenue.

Table 5: Corporate
Income Tax Loss

| Tax Year | GR Loss |
|----------|-----------------|
| 2022 | (\$33,900,000) |
| 2023 | (\$76,500,000) |
| 2024 | (\$119,100,000) |
| 2025 | (\$139,100,000) |
| 2026 | (\$139,100,000) |

This proposed legislation could create a situation in which a pass-through business could decide to file as a corporation instead of under the Individual Income Tax rate. Currently, SB 509 is estimated to make changes to the individual income tax rate as well as changes to the business income exemption. In order to calculate the difference between the current impact and the impact under this proposed legislation we have included those changes in the calculations. An example of new businesses started in Tax Year 2022 is included as an example.

Table 6: Pass-Through Income Tax Impacts for Businesses
Started in Tax Year 2022*

| Year of Operation | Number of Businesses | Current Estimated Taxes** | Proposed Estimated Taxes*** | Difference in Taxes Owed |
|-------------------|----------------------|---------------------------|-----------------------------|--------------------------|
| 1 | 14,642 | \$23,451 | \$7,699 | (\$15,752) |
| 2 | 12,264 | \$28,803 | \$6,738 | (\$22,065) |
| 3 | 12,264 | \$28,803 | \$10,869 | (\$17,934) |
| 4 | 8,637 | \$42,142 | \$24,313 | (\$17,829) |
| 5 | 8,637 | \$41,331 | \$32,417 | (\$8,914) |

*This is only the tax structure for businesses started in 2022.

**The estimates for current taxes accounts for the top rate reductions and business income exemptions under SB 509 (2014).

***The estimates for proposed taxes accounts for the business income exemptions under SB 509 (2014).

The total impact estimated of all pass-through businesses beginning in the first five (5) years of this proposal are:

Table 7: Individual
Income Loss

| Tax Year | GR Loss |
|-------------|-----------------|
| 2022 | (\$230,641,824) |
| 2023 | (\$501,244,825) |
| 2024 | (\$721,184,752) |
| 2025 | (\$833,544,841) |
| 2026 | (\$884,896,400) |

This would result in a combined loss of the Corporate and Individual Income Tax to GR by tax year:

Table 6: Summary of GR
Impact

| Tax Year | GR Loss |
|-------------|-------------------|
| 2022 | (\$264,541,824) |
| 2023 | (\$577,744,825) |
| 2024 | (\$840,284,752) |
| 2025 | (\$972,644,841) |
| 2026 | (\$1,023,996,400) |

DOR uses a 42%/58% split when converting tax years to fiscal years for Individual Income Tax and a 50%/50% split for corporate tax. Therefore the fiscal year impact would be:

| Table 9: Summary of GR Impact | |
|-------------------------------|-------------------|
| Fiscal Year | GR Loss |
| 2022 | (\$113,819,566) |
| 2023 | (\$382,545,084) |
| 2024 | (\$653,169,594) |
| 2025 | (\$837,925,989) |
| 2026 | (\$924,662,496) |
| 2027 | (\$1,023,996,400) |

This proposed legislation would require an entire separate regime to impose a separate rate of taxes. This would involve programming changes and possible new FTEs. This proposed legislation requires DOR to have the burden of ensuring compliance to determine which year of operation the business is in. There currently are not any solid resources to confirm that determination. Therefore, new forms, programming and staff would be needed. At this time the exact fiscal impact, as it relates to administration, is unknown.

DOR anticipates that this proposed section would require a totally new program that would require DOR to contract with a provider. DOR believes the fiscal impact for this could be greater than \$1 million. DOR will continue to research and update when needed.

DOR assumes it will need at least 3 additional Auditors to start. Depending on the number of audits required to ensure compliance, the number of auditors could increase in future years.

For purposes of this fiscal note, Oversight will report the impact to GR as a result of the Income Tax changes, as reported by B&P.

In addition, for the purposes of this fiscal note, Oversight will report the \$1 million contract cost and the three (3) FTE Auditors required by the Missouri Department of Revenue. Oversight notes the \$1 million will be included in DOR's equipment & expense.

DOR states Section 143.513 allows DOR to extend the deadline for filing of a corporation or other business entity's income tax return for a period of up to a year for those with Missouri taxable income of less than \$5,000. It should be noted that the language of this section would only allow the extension of the filing deadline and not the deadline for paying taxes. Since the businesses would need to complete their return in order to determine the correct tax amount to pay, it is assumed few businesses may ask for an extension.

This section also prohibits the assessment of interest or penalties during the extension period. It should be noted that penalties are not assessed on the filing of the return but on the payment amount not being submitted in a timely manner.

If this section is meant to extend both the filing deadline and the payment deadline, DOR is unable to determine how we could administer this provision. A company would need to calculate their taxable income before they could request an extension and DOR would need that information before providing the extension. This would result in additional tax filing forms, additional filing deadlines and increased computer programming costs that could exceed several hundred thousand dollars.

For purposes of this fiscal note, Oversight will report a \$100,000 cost for additional deadlines, additional tax filings, and increased computer programming. Oversight notes the cost will be included in DOR's equipment & expense.

Oversight notes that it **does not currently have the resources and/or access to state tax data** to produce an independent revenue estimate and is unable to verify the revenue estimates provided by B&P and DOR.

Section 431.203 – Non-Compete Agreements

Officials from **B&P** state this section would prohibit non-compete agreements and would make any existing non-compete agreements void as of August 28, 2021. This section will not impact TSR or the calculation under Article X, Section 18(e).

Officials from the **DOR** do not anticipate this section will result on a fiscal impact on their organization. Oversight does not have any information to the contrary. Therefore, Oversight will not report a fiscal impact for this organization as it relates to this section.

Section 620.3800 – Office of Entrepreneurship

Officials from **B&P** state this section would create the "Office of Entrepreneurship" under DED. The General Assembly may appropriate funds from the SSBCI to fund the newly created office. This section will not impact TSR or the calculation under Article X, Section 18(e).

Officials from the **DOR** do not anticipate this section will result in a fiscal impact on their organization. Oversight does not have any information to the contrary. Therefore, Oversight will not report a fiscal impact for this organization as it relates to this section.

Officials from the **Office of the Secretary of State (SOS)** note many bills considered by the General Assembly include provisions allowing or requiring agencies to submit rules and regulations to implement the act. 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 SOS for administrative rules is less than \$5,000. SOS recognizes that this is a small amount and does not expect that additional funding would be required to meet these costs. However, 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 SOS can sustain with SOS's core budget. Therefore, 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 proposed legislation. If multiple bills pass which require the printing and distribution of regulations at substantial costs, the SOS could request funding through the appropriations process.

Officials from the **Joint Committee on Administrative Rules** assume this proposal is not anticipated to cause a fiscal impact beyond its current appropriation.

Oversight assumes JCAR will be able to administer any rules from this proposed legislation with existing resources.

Officials from the **Missouri Department of Agriculture**, the **Missouri State Treasurer's Office** and the **Missouri Department of Transportation** do not anticipate this proposed legislation will cause a fiscal impact on their organization. Oversight does not have any information to the contrary. Therefore, Oversight will not report a fiscal impact for these organizations.

Oversight notes not all agencies requested to respond for this fiscal note have provided response to date.

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.

| <u>FISCAL IMPACT – State Government</u> | FY 2022 (10 Mo.) | FY 2023 | FY 2024 | Fully Implemented (FY 2027) |
|--|---|---|---|---|
| GENERAL REVENUE | | | | |
| <u>Revenue Reduction – Section 30.750 – Lost Opportunity For Higher Returns</u> | Less than or greater than (\$49,492) | Less than or greater than (\$49,492) | Less than or greater than (\$49,492) | Less than or greater than (\$49,492) |
| <u>Revenue Reduction – Section(s) 143.073 & 143.513 – Income Tax Changes p. 12, 17</u> | (\$113,819,566) | (\$399,495,084) | (\$691,419,595) | (\$1,023,996,400) |
| <u>Cost – DOR</u> | | | | |
| Personnel Services | (\$111,960) | (\$135,696) | (\$137,052) | (\$141,205) |
| Fringe Benefits | (\$67,637) | (\$81,617) | (\$82,075) | (\$83,477) |
| Equipment & Expense | (\$1,129,134) | (\$1,473) | (\$1,509) | (\$1,626) |
| Total Cost – DOR p. 17 | (\$1,308,731) | (\$218,786) | (\$220,636) | (\$226,308) |
| FTE Change – DOR | 3 FTE | 3 FTE | 3 FTE | 3 FTE |
| ESTIMATED NET EFFECT ON GENERAL REVENUE | <u>Less than or greater than (\$115,177,789)</u> | <u>Less than or greater than (\$399,763,362)</u> | <u>Less than or greater than (\$691,689,723)</u> | <u>Less than or greater than (\$1,024,272,200)</u> |
| | | | | |
| | | | | |

| | | | | |
|---|--|--|--|--|
| OTHER STATE FUNDS | | | | |
| | | | | |
| <u>Revenue Reduction – Section 30.750 – Lost Opportunity For Higher Returns</u> | <u>Less than or greater than (\$77,411)</u> | <u>Less than or greater than (\$77,411)</u> | <u>Less than or greater than (\$77,411)</u> | <u>Less than or greater than (\$77,411)</u> |
| | | | | |
| ESTIMATED NET EFFECT ON OTHER STATE FUNDS | <u>Less than or greater than (\$77,411)</u> | <u>Less than or greater than (\$77,411)</u> | <u>Less than or greater than (\$77,411)</u> | <u>Less than or greater than (\$77,411)</u> |

| | | | | |
|---|---------------------|-------------------|-------------------|-----------------------------------|
| <u>FISCAL IMPACT – Local Government</u> | FY 2022 (10 Mo.) | FY 2023 | FY 2024 | Fully Implemented (FY 2027) |
| | | | | |
| | <u>\$0</u> | <u>\$0</u> | <u>\$0</u> | <u>\$0</u> |

FISCAL IMPACT – Small Business

This proposed legislation could impact any small business that could receive a linked deposit and any small business that qualifies for the lower tax rate(s) put forth in this proposed legislation.

FISCAL DESCRIPTION**LINKED DEPOSITS (Section 30.750, RSMo)**

This bill adds to the definition of "eligible small business", a person who receives a loan from the Small Business Administration; however, a person eligible under this bill will not receive a linked deposit in an amount more than 10% of the amount of the loan from the Small Business Administration or \$250,000, whichever is less, and, if such person relocates out of this state within 10 years of receiving the linked deposit, the person will be required to repay the interest forgone on the linked deposit rate to the state.

STATE CONTRACTS (Section 34.195)

Under this bill, 5% of all state contracts will be awarded to businesses that have been in operation for less than five years.

RIGHT TO START ACT (Sections 143.073 and 143.513)

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

This bill creates the "Right to Start Act".

For all tax years beginning on or after January 1, 2022, a tax is imposed upon the Missouri taxable income of an eligible corporation or other business entity, validly licensed under the applicable laws of this state, which begins business operations in this state on or after the effective date of this bill, as follows:

For the first tax year of an eligible new business, the first \$250,000 of income will be exempt from taxation and any remaining portion of income will be taxed at a rate of 4%;

For the second tax year of an eligible new business, the first \$500,000 of income will be taxed at a rate of 1% and any remaining portion of income will be taxed at a rate of 4%;

For the third tax year of an eligible new business, the first \$750,000 of income will be taxed at a rate of 2% and any remaining portion of income will be taxed at a rate of 4%;

For the fourth tax year of an eligible new business, the first \$1 million dollars of income will be taxed at a rate of 3% and any remaining portion of income will be taxed at a rate of 4%;

For the fifth tax year of an eligible new business and for all tax years thereafter, all income will be taxed at a rate of 4%.

The income tax imposed under this bill will be imposed on eligible new businesses in lieu of the income tax otherwise imposed under Sections 143.011, 143.021, and 143.071, and any other provisions of Chapter 143.

For all tax years beginning on or after January 1, 2022, for any taxpayer who is a corporation or other business entity, validly licensed under the applicable laws of this state and with a Missouri taxable income of less than \$5,000 for the tax year, the Department of Revenue may extend the deadline for the filing of such taxpayer's income taxes and tax returns for a period of one year, at which time such taxes and tax returns must be filed along with any taxes and tax returns otherwise due for the tax year in which the extension ends.

No interest or late penalty will be assessed under any provision of law for individual, corporate, or eligible small business income taxes or income tax returns in which the filing deadline is extended under this bill, provided that, such taxes and tax returns are filed before the extended deadline.

The Department of Revenue may design any forms and may promulgate any necessary rules and regulations for the administration of this extension. Such rules will include, but not be limited to, rules describing how eligible taxpayers will apply for the extension allowed under this bill, how the applications for the extension will be processed by the Department, and how taxpayers who are awarded an extension will file taxes after the extension ends.

NON-COMPETE AGREEMENTS (Section 431.203)

This bill prohibits and voids agreements, understandings, contracts, or contractual terms in which an employee or prospective employee agrees not to compete against an employer or prospective employer or agrees not to accept any positions with a competitor of an employer or prospective employer following the termination of a business or employment relationship between the employee or prospective employee and the employer or prospective employer. Such agreements will be unenforceable and may, but need not, contain time-based or geographic limitations.

OFFICE OF ENTREPRENEURSHIP (Section 620.3800)

This bill creates an Office of Entrepreneurship within the Department of Economic Development. The office will be funded subject to appropriation from the federal State Small Business Credit Incentive (SSBCI) funds.

SOURCES OF INFORMATION

Office of Administration – Budget & Planning Division

Missouri Department of Revenue

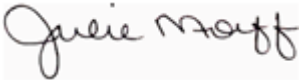
Missouri Department of Agriculture

Missouri Department of Transportation

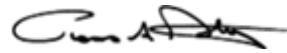
Missouri Secretary of State's Office

Missouri State Treasurer's Office

Joint Committee on Administrative Rules



Julie Morff
Director
March 3, 2021



Ross Strobe
Assistant Director
March 3, 2021