COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 0903H.02C
Bill No.: HCS for HB 356
Subject: Taxation and Revenue - General; Taxation and Revenue - Income; Department of Revenue; Retirement Systems and Benefits - General
Type: Original
Date: March 1, 2023

Bill Summary: This proposal modifies provisions relating to income tax deductions for private pensions.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND			
FUND AFFECTED	FY 2024	FY 2025	FY 2026
General Revenue Fund*	$0	($94,242,727)	($92,279,337)
Total Estimated Net Effect on General Revenue	**$0**	**($94,242,727)**	**($92,279,337)**

*The fiscal note reflects the assumptions that the SB 3 (2022) reductions are triggered consecutively.

ESTIMATED NET EFFECT ON OTHER STATE FUNDS			
FUND AFFECTED	FY 2024	FY 2025	FY 2026
Total Estimated Net Effect on Other State Funds	**$0**	**$0**	**$0**

Numbers within parentheses: () indicate costs or losses.

ESTIMATED NET EFFECT ON FEDERAL FUNDS			
FUND AFFECTED	FY 2024	FY 2025	FY 2026
Total Estimated Net Effect on All Federal Funds	**$0**	**$0**	**$0**

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)			
FUND AFFECTED	FY 2024	FY 2025	FY 2026
Total Estimated Net Effect on FTE	**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 2024	FY 2025	FY 2026
Local Government	**$0**	**$0**	**$0**

FISCAL ANALYSIS

ASSUMPTION

Section 143.124 Retirement Income Tax Deduction

Officials from the **Department of Revenue (DOR)** note this proposal is changing the taxability of retirement income. Currently, depending on the type of retirement benefit and the taxpayer's Missouri adjusted gross income (MAGI) some of the benefits are taxable.

Public Retirement Benefits
Per statutes, any retirement benefits other than public pension benefits are eligible to receive up to the first $6,000 in income from retirement benefits as an exemption from taxation. This would include pensions from private companies, 401(k), deferred compensation plans, annuities, and self-employed retirement plans (Keogh). This exemption is only allowed for individual taxpayers with a MAGI of less than $25,000 or for those filing a combined return of up to $32,000 MAGI.

Starting January 1, 2024, this proposal would increase the $6,000 to $12,000 for taxpayers. It would also increase the number of people eligible for this exemption by increasing the MAGI of individual filers to $50,000 and the MAGI of combined filers to $64,000. This will increase the number of people eligible for this exemption.

Impact
The Department notes these changes are to begin for tax years starting January 1, 2024, and therefore will not fiscally impact the state until FY 2025 based on when the tax returns are filed claiming the exemption.

DOR officials used information reported by taxpayers on their federal returns to start the calculation of the additional revenue that may be exempt from tax. Then DOR used its internal Individual Income Tax Database for Missouri. DOR found the following distribution of filers of public and private pensions.

Pensions	Public	Private
Singles	39%	61%
Married Filing Joint	49%	51%
Head of Household (HOH)	42%	58%

Below is the estimated loss per benefit type:

Estimated Loss by Retirement Income

Retirement Income	4.95%	4.80%	4.70%	4.60%	4.50%
Individual Retirement Distributions	($37,803,249)	($36,657,696)	($35,893,994)	($35,130,292)	($34,366,590)
Pensions/Annuities (Private)	($58,933,237)	($57,147,381)	($55,956,811)	($54,766,240)	($53,575,670)
Self-Employed (Keogh)	($451,327)	($437,650)	($428,532)	($419,415)	($410,297)
Total GR Loss	**($97,187,813)**	**($94,242,727)**	**($92,279,337)**	**($90,315,947)**	**($88,352,557)**

SB 3 adopted in 2022 set the individual income tax rate at 4.95% in tax year 2023. The tax rate is scheduled to continue to reduce over a period of several years until the rate equals 4.5%. At that time, it will remain the 4.5%. Since this proposal begins with tax year 2024, (FY 2025) the rate is estimated to be 4.8%. For fiscal note purposes, DOR will show the loss at each of those tax rates over SB 3's implementation period. This will result in a loss to general revenue. DOR estimates the loss to general revenue:

Estimated Loss by Fiscal Year

	Tax Year (Fiscal Year)			
Tax Rate	2024 (FY25)	2025 (FY26)	2026 (FY27)	2027 (FY28)
4.95%	($97,187,813)	($97,187,813)	($97,187,813)	($97,187,813)
4.80%	($94,242,727)	($94,242,727)	($94,242,727)	($94,242,727)
4.70%		($92,279,337)	($92,279,337)	($92,279,337)
4.60%			($90,315,947)	($90,315,947)
4.50%				($88,352,557)

Administrative Impact
This proposal will require modification to the MO-A form and to the MO-1040P form. Additionally DOR will need to modify its website and its individual income tax computer system. These changes are estimated to cost $7,193.

At this time, the Department believes it can handle this work with existing resources. However, should the department reach the number of errors or correspondence to justify additional FTE from this proposal or in combination with other proposals that will pass, it will seek the required number of FTE through the appropriation process. The Department is providing the number of errors or correspondence that require additional FTE.

1 FTE Associate Customer Service Rep for every 14,700 errors created
1 FTE Associate Customer Service Rep for every 5,700 pieces of correspondence generated

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 administrative 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:

Individual Retirement Distributions
Currently taxpayers may subtract $6,000 of their individual retirement income, if their Missouri Adjusted Gross Income (MAGI) is less than $25,000 for taxpayers filing single or head of household and $32,000 for married filing combined taxpayers. B&P notes that these payments would include IRAs and 401(k) plans.

B&P notes this proposal would allow taxpayers to subtract $12,000 of their retirement income, if their MAGI is less than $50,000 for singles and $64,000 for married filing combined taxpayers.

Based on data published by the IRS, B&P estimates that this provision may exempt up to $356,706,746 in individual retirement arrangement payments for taxpayers filing single, $119,123,284 for taxpayers filing head of household, and $366,736,152 for married filing joint taxpayers; for a total of up to $763,701,991 in income exempted under this section.

However, exemptions do not reduce revenues on a dollar for dollar basis, but rather in proportion to the top tax rate applied. Therefore, B&P will show the estimated impacts throughout the implementation of the tax rate reductions from SB 3 (2022). Consequently, B&P estimates that exempting individual retirement arrangement payments could reduce TSR and GR by $37,803,249 (top tax rate 4.95%) or by $36,657,696 (top tax rate 4.8%) in FY25. Once SB 3 (2022) has fully implemented, this provision could reduce TSR and GR by $34,366,590 annually.

Pensions and Annuities
B&P notes that the term "pensions and annuities" includes both public and private retirement funds. For the purpose of this fiscal note, B&P used tax year 2020 (the most recent complete year available) Missouri tax return data to estimate the percentage of payments from public pensions and annuities versus private pensions and annuities.

In tax year 2020, 61% of pension and annuity payments were from private funds and 39% were from public funds for individuals filing single. For married filing combined individuals, 51% of payments were from private funds, while 49% were from public funds. For taxpayers filing as head of household, 58% of pension and annuity payments were from private sources, while 42% were from public sources.

Private Pensions and Annuities
Currently taxpayers may exempt $6,000 of their private pension and annuity income, if their Missouri Adjusted Gross Income (MAGI) is less than $25,000 for taxpayers filing single or head of household and $32,000 for married filing combined taxpayers.

B&P notes this proposal would allow taxpayers to subtract $12,000 of their retirement income, if their MAGI is less than $50,000 for singles and $64,000 for married filing combined taxpayers.

Based on data published by the IRS, B&P estimates that this provision may exempt up to $749,989,260 in private pension and annuity payments for taxpayers filing single, $231,810,834 for taxpayers filing head of household, and $509,493,355 for married filing joint taxpayers; for a total of up to $231,810,834 in income exempted under this section.

However, exemptions do not reduce revenues on a dollar for dollar basis, but rather in proportion to the top tax rate applied. Therefore, B&P will show the estimated impacts throughout the implementation of the tax rate reductions from SB 3 (2022). Consequently, B&P estimates that exempting individual retirement arrangement payments could reduce TSR and GR by $58,933,237 (top tax rate 4.95%) or by $57,147,381 (top tax rate 4.8%) in FY25. Once SB 3 (2022) has fully implemented, this provision could reduce TSR and GR by $53,575,670 annually.

Self-Employed (Keogh) Payments
B&P notes currently taxpayers may exempt $6,000 of their Keogh retirement income, if their Missouri Adjusted Gross Income (MAGI) is less than $25,000 for taxpayers filing single or head of household and $32,000 for married filing combined taxpayers.

This proposal would allow taxpayers to subtract $12,000 of their retirement income, if their MAGI is less than $50,000 for singles and $64,000 for married filing combined taxpayers.

B&P notes based on data published by the IRS, B&P estimates that this provision may exempt $3,566,765 in Keogh payments for taxpayers filing single, $1,160,709 for taxpayers filing head of household, and $5,160,139 for married filing joint taxpayers; for a total of $1,160,709 in income exempted under this section.

However, exemptions do not reduce revenues on a dollar for dollar basis, but rather in proportion to the top tax rate applied. Therefore, B&P will show the estimated impacts throughout the implementation of the tax rate reductions from SB 3 (2022). Consequently, B&P estimates that exempting individual retirement arrangement payments could reduce TSR and GR by $451,327 (top tax rate 4.95%) or by $437,650 (top tax rate 4.8%) in FY25. Once SB 3 (2022) has fully implemented, this provision could reduce TSR and GR by $410,297 annually.

Summary
B&P estimates that this proposal could reduce TSR and GR by $97,187,813 (top tax rate 4.95%) or by $94,242,727 (top tax rate 4.8%) in FY25. Once SB 3 (2022) has fully implemented, this proposal could reduce TSR and GR by $88,352,557 annually. Table 1 shows the estimated loss by provision, while Table 2 shows the estimated loss by tax and fiscal year.

Table 1: Estimated Loss by Retirement Income

Retirement Income	4.95%	4.8%	4.7%	4.6%	4.5%
Individual Retirement Distributions	($37,803,249)	($36,657,696)	($35,893,994)	($35,130,292)	($34,366,590)
Pensions/Annuities (Private)	($58,933,237)	($57,147,381)	($55,956,811)	($54,766,240)	($53,575,670)
Self-Employed (Keogh)	($451,327)	($437,650)	($428,532)	($419,415)	($410,297)
Total GR Loss	**($97,187,813)**	**($94,242,727)**	**($92,279,337)**	**($90,315,947)**	**($88,352,557)**

Table 2: Estimated Loss by Fiscal Year

	Tax Year (Fiscal Year)			
Tax Rate	2024 (FY25)	2025 (FY26)	2026 (FY27)	2027 (FY28)
4.95%	($97,187,813)	($97,187,813)	($97,187,813)	($97,187,813)
4.80%	($94,242,727)	($94,242,727)	($94,242,727)	($94,242,727)
4.70%		($92,279,337)	($92,279,337)	($92,279,337)
4.60%			($90,315,947)	($90,315,947)
4.50%				($88,352,557)

Oversight notes both DOR and B&P's estimates include data from DOR and B&P's internal Income Tax Model.

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 DOR's and B&P's estimated impact for this proposal. For the purpose of this fiscal note, Oversight will reflect the assumption that the SB 3 (2022) reductions are triggered consecutively.

FISCAL IMPACT – State Government	FY 2024 (10 Mo.)	FY 2025	FY 2026
GENERAL REVENUE FUND			
Revenue Reduction - §143.124 – Retirement Income Tax Deduction	$0	($94,242,727)	($92,279,337)
ESTIMATED NET IMPACT ON GENERAL REVENUE FUND	**$0**	**($94,242,727)**	**($92,279,337)**

FISCAL IMPACT – Local Government	FY 2024 (10 Mo.)	FY 2025	FY 2026

	$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

The proposed legislation modifies provisions relating to income tax deductions for private pensions.

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
March 1, 2023

Ross Strope
Assistant Director
March 1, 2023