

COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 1679H.011
 Bill No.: HB 499
 Subject: Economic Development, Department Of; Tax Credits; Tax Incentives; Business
 And Commerce
 Type: Original
 Date: February 3, 2025

Bill Summary: This proposal establishes Earnings Tax Opportunity Zones.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND			
FUND AFFECTED	FY 2026	FY 2027	FY 2028
General Revenue*	Less than \$4,619,744	Less than \$13,859,231	Less than \$13,859,231
Total Estimated Net Effect on General Revenue	Less than \$4,619,744	Less than \$13,859,231	Less than \$13,859,231

*A reduction in earnings taxes collected by St. Louis City and Kansas City, would reduce the amount of deductions used in calculating Missouri’s state income tax, thereby increasing state income tax collections (or reducing state tax refunds). Oversight assumes the actual impact may be significantly less depending on the number of taxpayers that qualify for exemption of the earnings tax.

ESTIMATED NET EFFECT ON OTHER STATE FUNDS			
FUND AFFECTED	FY 2026	FY 2027	FY 2028
Total Estimated Net Effect on <u>Other</u> State Funds	\$0	\$0	\$0

Numbers within parentheses: () indicate costs or losses.

ESTIMATED NET EFFECT ON FEDERAL FUNDS			
FUND AFFECTED	FY 2026	FY 2027	FY 2028
Total Estimated Net Effect on <u>All</u> Federal Funds	\$0	\$0	\$0

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)			
FUND AFFECTED	FY 2026	FY 2027	FY 2028
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 2026	FY 2027	FY 2028
Local Government*	Less than (\$225,006,667)	Less than (\$607,520,000)	Less than (\$607,520,000)

*The fiscal impact depends on the number of taxpayers who live in and/or work in Opportunity Zones and qualify for the exemption of the earnings tax. Therefore, Oversight assumes the actual impact may be significantly less.

FISCAL ANALYSIS

ASSUMPTION

§92.205 – Earnings Tax Opportunity Zones

Officials from the **Office of Administration - Budget and Planning (B&P)** assume this proposal would exempt all individual and business earnings from the earnings and payroll taxes levied by St. Louis City and Kansas City for certain areas beginning tax year 2025. B&P notes that this proposal would start tax year 2025 but become effective August 28, 2025 – in the middle of tax year 2025. B&P further notes that while earnings tax returns are not due until January of the next year, many city residents have the 1% tax withheld from their paychecks. B&P assumes that St. Louis City and Kansas City will be required to refund any withheld earnings collections received from January 2025 through August 2025.

To qualify, an area must be in an opportunity zone, with median income under 70% of the metropolitan statistical area (MSA) and with a poverty rate of 20% or higher.

B&P is unable to determine how much of either city's earnings, payroll, and profit taxes are derived from qualifying areas. For the purpose of this fiscal note, B&P will show the potential impact as "up to" the total amount of taxes collected. B&P notes that the actual impact may be significantly less.

Based on data published by St. Louis City¹, in FY23 the city collected \$173,595,000 in individual earnings tax and \$107,431,000 in business earnings/payroll taxes. Based on data published by Kansas City², in FY24 the city collected \$252,728,000 in earnings tax and \$73,766,000 in profits tax.

B&P notes that individuals and businesses can deduct the taxes paid to the city on their Missouri state income tax. Based on 2022 tax return data, B&P determined that 28.8% of individual itemize their return. For the purpose of this fiscal note, B&P assumes that 100% of businesses also deduct these taxes. In addition, B&P apportioned out the taxes paid by businesses between corporations (49.7%) and pass-through (50.3%) businesses, based on annual payroll data published by the U.S. Census Bureau, in order to determine the correct state income tax rate.

Therefore, B&P estimates that this proposal could increase GR by up to \$13,431,413 to \$13,859,231 (depending on the individual income tax rate applied). This proposal could reduce revenues to St. Louis City by up to (\$281,026,000) and revenues to Kansas City by up to (\$326,494,000). Table 1 shows the estimated impact by local tax. Table 2 shows the estimated impact to GR by tax/fiscal year.

¹ <https://www.stlouis-mo.gov/government/departments/comptroller/investor-relations/city-information/Current-CAFR.cfm>, FY23 CAFR – Table 9, page 216

² <https://drive.google.com/drive/folders/1AMRH4z6Mbjr6LRmEcOFiYUfkaZ-An4CT>, FY24 CAFR – Table 9, page 422-423

Table 1: Estimated Impact by Tax

<u>St. Louis City</u>		<u>GR Impact</u>			<u>Local Impact</u>
		<u>Low</u>	<u>High</u>		
Individual Earnings Tax	Up to	\$2,249,791	\$2,349,782	Up to	(\$173,595,000)
Business Earnings Tax	Up to	\$2,500,454	\$2,559,612	Up to	(\$58,814,000)
Payroll Tax	Up to	\$2,269,681	\$2,318,582	Up to	(\$48,617,000)
Total St. Louis City	Up to	\$7,019,926	\$7,227,976	Up to	(\$281,026,000)
<u>Kansas City</u>					
Earnings Tax	Up to	\$3,275,355	\$3,420,926	Up to	(\$252,728,000)
Profits Tax	Up to	\$3,136,132	\$3,210,329	Up to	(\$73,766,000)
Total Kansas City	Up to	\$6,411,487	\$6,631,255	Up to	(\$326,494,000)
<hr/>					
Estimated Impact	Up to	\$13,431,413	\$13,859,231	Up to	(\$607,520,000)

Table 2: Estimated GR Impact by Year

Tax Rate	2025 (FY26)	2026 (FY27)	2027 (FY28)	2028 (FY29)
4.70%	\$13,859,231	\$13,859,231	\$13,859,231	\$13,859,231
4.60%		\$13,645,322	\$13,645,322	\$13,645,322
4.50%			\$13,431,413	\$13,431,413

*Up to the estimates shown.

Officials from the **Department of Revenue (DOR)** assume the City of Kansas City and the City of St. Louis are allowed to assess an “earnings tax” on citizens or businesses working in their city limits. The tax rate is 1%. Information published by these cities indicates that in FY 2023, the City of St. Louis collected \$173,595,000 in individual earnings tax and \$107,431,000 in business earnings/payroll taxes. Kansas City collected \$252,728,000 in earnings tax and \$73,766,000 in profit tax.

Beginning with tax years starting January 1, 2024, this would allow all individuals and businesses in a “earnings tax opportunity zone” to be exempt from paying the earning tax to their city. It should be noted that this proposal would not become effective until August 28, 2025, but is attempting to make this exemption retroactive to January 1, 2024. It should be noted that while earnings tax is not due until the following January, many of the required payors ask to have money withheld monthly to make the payments. This could result in Kansas City and St. Louis needing to refund earnings tax already collected from January 1, 2024, to August 28, 2025.

DOR is unable to determine which businesses or citizens currently live or work in one of these “earnings tax opportunity zones”. For fiscal note purposes only, DOR will show the impact up to the total amount of taxes these cities currently collect.

Taxes paid to state and local government can be itemized on a taxpayer’s individual income tax return. Using DOR’s internal individual income tax system, DOR was able to determine that approximately 28.8% of all people itemize. For fiscal note purposes, DOR will be assuming that 100% of the eligible companies would be exempt. Using DOR’s confidential income tax data, DOR knows that DOR can apportion the business funding to 50.3% to corporations and 49.7% to pass-through businesses.

DOR notes this proposal could reduce revenues to St. Louis City up to (\$281,026,000) and revenues to Kansas City up to (\$326,494,000). When the citizens and businesses no longer owe this tax to the cities, they will no longer be able to subtract it off their MO individual income tax return. Therefore, general revenue may see an increase up to \$13,431,413 to \$13,859,231 (depending on the individual income tax rate applied). SB 3 adopted in 2022 allows the individual income tax rate to decrease based on certain revenue triggers being met. Currently for tax year 2025 the rate is 4.7% but can drop to 4.5% over a period of years. DOR will show the impact over the rate decreases of SB 3.

Table 1 shows the estimated impact by local tax.

Table 1: Estimated Impact by Tax					
		GR Impact			Local Impact
		Low	High		
St. Louis City					
Individual Earnings Tax	Up to	\$2,249,791	\$2,349,782	Up to	(\$173,595,000)
Business Earnings Tax	Up to	\$2,500,454	\$2,559,612	Up to	(\$58,814,000)
Payroll Tax	Up to	\$2,269,681	\$2,318,582	Up to	(\$48,617,000)
Total St. Louis City	Up to	\$7,019,926	\$7,227,976	Up to	(\$281,026,000)
Kansas City					
Earnings Tax	Up to	\$3,275,355	\$3,420,926	Up to	(\$252,728,000)
Profits Tax	Up to	\$3,136,132	\$3,210,329	Up to	(\$73,766,000)
Total Kansas City	Up to	\$6,411,487	\$6,631,255	Up to	(\$326,494,000)
Estimated Impact	Up to	\$13,431,413	\$13,859,231	Up to	(\$607,520,000)

Table 2 shows the estimated impact to GR by tax/fiscal year.

Table 2: Estimated GR Impact by Year				
Tax Rate	2025 (FY26)	2026 (FY27)	2027 (FY28)	2028 (FY29)
4.70%	\$13,859,231	\$13,859,231	\$13,859,231	\$13,859,231
4.60%		\$13,645,322	\$13,645,322	\$13,645,322
4.50%			\$13,431,413	\$13,431,413

*Up to the estimates shown.

Officials for **St. Louis City** state the following:

The proposed legislation would eliminate the Earnings Tax on Individuals working and businesses operating within defined Opportunity zone clusters and qualified census tracts as defined under respective U.S. codes. No actual earnings tax data from these portions of the City are currently available. However, estimates can be made drawing upon data from the 2018-2022 American Community Survey 5-year estimates published by the U.S. Census Bureau. Based on this survey data there are 27 census tracts which would fall under the proposed zones with an estimated annual income total of over \$1.4 billion. This does not include businesses operating in these areas. With the Earnings tax at 1%, the potential loss in revenue could be expected to be a minimum of \$15 million per year.

Adding significantly to this loss, however, is the pending relocation of the National Geospatial-Intelligence Agency (NGA) from its current location in the Soulard Neighborhood of the City into one of these impacted census tracts. The NGA project is a \$1.7 billion construction project serving as a catalytic development to the region. City and the surrounding neighborhoods. This development was made possible in part by a cooperative funding agreement between the City and State of Missouri that secured the retention of this key employer with over 3,100 workers within the City and State. The equivalent of the Earnings taxes generated by the employees of NGA was utilized as a basis of the financing agreement and the elimination of these revenues would undermine the spirit of this agreement. In 2021, it was estimated that the Earnings Tax receipts generated by NGA workers in the City totaled \$3.5 million. As the NGA relocation is anticipated to be completed in 2026, these revenues would also be lost under the legislative proposal.

Total combined loss would be in the range of \$20 million annually.

In HB 499 current form, the legislation states “beginning on or after January 1, 2024, the following shall be exempt from the earnings tax imposed under sections 92.105 to 92.000...”. The plain language appears to require the City of St. Louis to refund any earnings tax paid on wages, commissions etc. earned within an opportunity zone for the calendar year of 2024 and 2025. If the City is required to refund earnings taxes associated with the defined opportunity zones, the estimated costs will increase by approximately \$22.5 million in addition to the annual \$20 million noted above.

Refunds Costs: \$22.5 million (assuming each eligible individual and business filed for a refund)
On-going costs: \$20 million
Total: \$42.5 million

The Earnings Tax is the City’s single largest source of revenue amounting to over a third of the General Fund budget. Total net receipts in FY24 were just under \$225.7 million. The proposed legislation would eliminate the tax within targeted census tracts and the potential loss of City revenue would be significant – having a negative impact on the City’s credit and fiscal condition and impairing the City’s ability to provide basic City services.

As a way of illustration – a potential loss of \$20 million of annual Earnings Tax revenue would be:

- Over 12% of the total FY24 general fund budget of the Police Department at \$164.4 million.

Or:

- Over 25% of the Fire Department budget of \$74.1 million

Or about the equivalent of these other City services:

- Forestry Division – Trimming/Weed & Debris - \$9.3 million
- Park Maintenance - \$10.6 million

Or:

- Street Maintenance & Repair - \$9.7 million
- Traffic & Street Lighting - \$11.7 million

Officials from **Kansas City** assume the proposed legislation will have a negative fiscal impact of an indeterminate amount.

Oversight does not have information to the contrary and therefore, Oversight will reflect the estimates as provided by the B&P, DOR, St. Louis City and Kansas City.

Oversight notes the legislation would go into effect, if enacted, on August 28, 2025. Therefore, there would be 4 months of CY 2025 where this proposal would exempt the earnings tax in these opportunity zones. Oversight will reflect 4 months for the exemption of earnings tax in FY26.

Oversight also notes this proposal may require the cities of St. Louis and Kansas City to refund earning tax that was collected from the taxpayers (both individual and business) since the proposal is, if enacted, taking the exemption date back to January 1, 2024. That would mean the earnings taxes collected from January 1, 2024 to August 28, 2025 would be eligible for refund. Therefore, Oversight will also show a potential revenue loss from refunds of the earnings tax in the Opportunity Zones of \$0 to unknown for this proposal.

Officials from the **Department of Economic Development** assume the proposal will have no fiscal impact on their organization. **Oversight** does not have any information to the contrary. Therefore, Oversight will reflect a zero impact in the fiscal note.

<u>FISCAL IMPACT – State Government</u>	FY 2026 (4 Mo.)	FY 2027	FY 2028
GENERAL REVENUE			
<u>Savings</u> – calculation of deductions relating to earnings tax that can no longer be itemized on state taxes §92.205 p. 5	<u>Less than</u> \$4,619,744	<u>Less than</u> \$13,859,231	<u>Less than</u> \$13,859,231
ESTIMATED NET EFFECT ON GENERAL REVENUE	<u>Less than</u> <u>\$4,619,744</u>	<u>Less than</u> <u>\$13,859,231</u>	<u>Less than</u> <u>\$13,859,231</u>

<u>FISCAL IMPACT – Local Government</u>	FY 2026 (4 Mo.)	FY 2027	FY 2028
ST. LOUIS CITY & KANSAS CITY			
<u>Costs</u> – potential refunds to taxpayers with earnings tax paid in from January 1, 2024 to August 28, 2025 (including the relocation of NGA in 2026 §92.205 p. 6-7	Could exceed (\$22,500,000)	\$0	\$0
<u>Revenue Loss</u> – potential loss in revenue from eliminating the Earnings Tax on Opportunity Zones in distressed communities §92.205 p. 5	<u>Less than</u> (\$202,506,667)	<u>Less than</u> (\$607,520,000)	<u>Less than</u> (\$607,520,000)
ESTIMATED NET EFFECT ON ST. LOUIS CITY AND KANSAS CITY FUNDS	<u>Less than</u> <u>(\$225,006,667)</u>	<u>Less than</u> <u>(\$607,520,000)</u>	<u>Less than</u> <u>(\$607,520,000)</u>

FISCAL IMPACT – Small Business

Small businesses who are in an Earning Tax Opportunity Zone could have an impact as a result of this proposal.

FISCAL DESCRIPTION

This bill establishes "earnings tax opportunity zones." These opportunity zones, as described in the bill, will correspond to existing federal census tracts described as "distressed communities". Beginning January 1, 2024, the following types of income will be exempt from the city earnings tax:

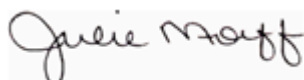
- (1) Salaries, wages, commissions, and other compensation earned by any resident of an earnings tax opportunity zone;
- (2) Salaries, wages, commissions, and other compensation earned by any person who earns salaries, wages, commissions, and other compensation for work done or services performed or rendered in an earnings tax opportunity zone;
- (3) Net profits of associations, businesses, or other activities conducted by any person in an earnings tax opportunity zone; and
- (4) Net profits earned by all corporations as the result of work done or services performed or rendered and business or other activities in an earnings tax opportunity zone.

If a distressed community that is found within an opportunity zone imposes a city earnings tax, that distressed community must publish and maintain an updated map of earnings tax opportunity zones on its website and provide a copy of the map upon request.

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

Office of Administration - Budget and Planning
Department of Revenue
Department of Economic Development
St. Louis City
Kansas City



Julie Morff
Director
February 3, 2025



Jessica Harris
Assistant Director
February 3, 2025