

COMMITTEE ON LEGISLATIVE RESEARCH  
OVERSIGHT DIVISION

**FISCAL NOTE**

L.R. No.: 1878H.01I  
Bill No.: HB 860  
Subject: Taxation and Revenue - Income; Taxation and Revenue - General; Employees - Employers; Department of Labor and Industrial Relations; Business and Commerce  
Type: Original  
Date: March 30, 2025

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Bill Summary: This proposal authorizes income tax deductions for employee compensation received as overtime pay or tips.

**FISCAL SUMMARY**

<b>ESTIMATED NET EFFECT ON GENERAL REVENUE FUND</b>			
<b>FUND AFFECTED</b>	<b>FY 2026</b>	<b>FY 2027</b>	<b>FY 2028</b>
General Revenue	(\$137,862,387 to \$390,947,314)	(\$134,847,662 to \$382,430,743)	(\$134,848,721 to \$382,431,802)
<b>Total Estimated Net Effect on General Revenue</b>	<b>(\$137,862,387 to \$390,947,314)</b>	<b>(\$134,847,662 to \$382,430,743)</b>	<b>(\$134,848,721 to \$382,431,802)</b>

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

Numbers within parentheses: () indicate costs or losses.

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

<b>ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)</b>			
<b>FUND AFFECTED</b>	<b>FY 2026</b>	<b>FY 2027</b>	<b>FY 2028</b>
General Revenue - DOR	1 FTE	1 FTE	1 FTE
<b>Total Estimated Net Effect on FTE</b>	<b>1 FTE</b>	<b>1 FTE</b>	<b>1 FTE</b>

- ☒ 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.

<b>ESTIMATED NET EFFECT ON LOCAL FUNDS</b>			
<b>FUND AFFECTED</b>	<b>FY 2026</b>	<b>FY 2027</b>	<b>FY 2028</b>
<b>Local Government</b>	<b>\$0</b>	<b>\$0</b>	<b>\$0</b>

## FISCAL ANALYSIS

### ASSUMPTION

#### **Section 143.121.3(14) - Individual Income Tax Subtraction – Overtime Income**

Officials from the **Department of Revenue (DOR)** note this proposal will allow a subtraction from federal adjusted gross income of 100 % of the overtime compensation a taxpayer receives. This proposal would become effective January 1, 2026, and the first returns claiming this subtraction would be filed starting January 1, 2027 (FY 2027).

Since there is no single source for overtime pay, DOR collected data from a couple sources. Based on a Gallup Poll released in 2021, 52% of all workers in the U.S. work more than the 40-hour workweek. The Bureau of Labor Statistics note Missouri has 2,875,146 workers who have an average hourly salary of \$29.68.

Current estimates indicate that 85% of all workers are exempt from the federal overtime laws under the Fair Labor Standards Act (FLSA). Employees who are executive, administrative, professional or outside sales employees that are paid a salary are exempt employees. However, in some instances an exempt employee may receive overtime pay. However, for the simplicity of the fiscal note, DOR will assume if you are an exempt employee, you will not receive overtime. An estimate of the number of Missouri workers by hours worked.

Table 1: Estimated MO Workers by Hours of Overtime						
Hours Worked	< 40 hrs	40 hrs	41-49	50-59	60-69	70+
% of workers	8%	40%	13%	21%	11%	7%
Est. # MO workers	230,012	1,150,058	373,769	603,781	316,266	201,260
Est. # MO Workers - exempt (85%)	230,012	1,150,058	317,704	513,214	268,826	171,071
Est. # MO Workers - Overtime Eligible	0	0	56,065	90,567	47,440	30,189

Therefore, DOR can assume that 230,012 workers could be receiving overtime pay and be eligible for this subtraction. Bringing the total number of hours of overtime paid to 146,442,686 to 248,481,618.

DOR notes that Missouri's minimum wage rate for 2024 is \$13.75 hour. BLS shows that Missouri has an average hourly salary of \$29.67. DOR will reflect a range of \$2,013,586,938 (minimum wage) to \$7,373,692,011 (BLS average). DOR notes that subtractions do not reduce revenue on a dollar for dollar basic but rather in proportion to the top tax rate applied. SB 3(2022) set the tax year 2025 individual income tax rate at 4.7%. SB 3 is projected to lower the rate to 4.5% over a period of years based on certain revenue growth. Therefore, DOR will show the impact over the implementation of SB 3.

Table 2: Estimated Revenue Loss by Fiscal Year

	Tax Year (Fiscal Year)					
Tax Rate	2026 (FY27)		2027 (FY28)		2028 (FY29)	
	Low	High	Low	High	Low	High
4.70%	(\$94,638,586)	(\$346,563,525)	(\$94,638,586)	(\$346,563,525)	(\$94,638,586)	(\$346,563,525)
4.60%			(\$92,624,999)	(\$339,189,833)	(\$92,624,999)	(\$339,189,833)
4.50%					(\$90,611,412)	(\$331,816,141)

This proposal will require changes to the department's MO-A form (\$2,200), its website and its individual income tax computer system (\$7,327). DOR assume the department would need one additional Associate Customer Service Representative (\$37,020) to handle this subtraction given the number of errors and correspondence that can be generated from these types of subtractions.

Officials from the **Office of Administration - Budget and Planning (B&P)** note this proposal would allow a 100% subtraction for overtime compensation included in a taxpayer's Federal Adjusted Gross Income (FAGI) when calculating their Missouri Adjusted Gross Income (MAGI). B&P notes that this proposal would become effective for tax year 2026.

Based on a 2021 Gallup poll, 52% of workers in the U.S. work more than 40 hours per week. According to BLS data, there were 2,875,146 workers in Missouri during 2023, with an average hourly wage of \$29.68.

In addition, current estimates indicate that approximately 85% of all workers are exempt from the federal overtime law. B&P notes that some individuals may receive overtime even if their position could be technically exempt from the federal law. However, for the purpose of this fiscal note, B&P will assume that individuals exempt under federal law will not receive overtime pay. This could understate the potential impact from this proposal. Table 1 shows the estimated breakdown of Missouri workers by hours worked.

Table 1: Estimated MO Workers by Hours of Overtime

	< 40					
Hours Worked	hrs	40 hrs	41-49	50-59	60-69	70+
% of workers	8%	40%	13%	21%	11%	7%
Est. # MO workers	230,012	1,150,058	373,769	603,781	316,266	201,260
Est. # MO Workers - exempt (85%)	230,012	1,150,058	317,704	513,214	268,826	171,071
Est. # MO Workers - Overtime Eligible	0	0	56,065	90,567	47,440	30,189

Therefore, B&P estimates that approximately 224,261 workers in Missouri may receive overtime pay. Based on the data above, B&P estimates that this provision could exempt 146,442,686 to 248,481,618 hours in overtime from state income tax.

B&P notes that per data published by the BLS, the average hourly wage in Missouri was \$29.64 in 2023. However, B&P notes that the federal overtime law has a maximum income below the annual average Missouri wages. Therefore, for the purpose of this fiscal note, B&P will calculate a range using the Missouri 2026 minimum wage of \$15.00 per hour and the BLS average wage of \$29.64 per hour.

Therefore, B&P estimates that this proposal may exempt \$2,196,640,295 to \$7,373,692,011 from state income tax. However, deductions 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). Table 2 shows the estimated impact by year.

Table 2: Overtime Income Tax Exemption - GR Impact

Tax Rate	Tax Year 2026		Tax Year 2027		Tax Year 2028	
	Low	High	Low	High	Low	High
4.70%	(\$103,242,094)	(\$346,563,525)	(\$103,242,094)	(\$346,563,525)	(\$103,242,094)	(\$346,563,525)
4.60%	(\$101,045,454)	(\$339,189,833)	(\$101,045,454)	(\$339,189,833)	(\$101,045,454)	(\$339,189,833)
4.50%			(\$98,848,813)	(\$331,816,141)	(\$98,848,813)	(\$331,816,141)

B&P notes that this proposal allows employers to stop withholding taxes immediately. Therefore, B&P estimates that this proposal could reduce TSR and GR in FY26 by \$50,522,727 to \$173,281,763. Once SB 3 (2022) has fully implemented, this proposal could reduce TSR and GR by \$98,848,813 to \$331,816,141 annually.

For additional information:

Using data provide by OA-Personnel, B&P estimates that in 2024 approximately \$118,688,496 was paid to state workers for overtime. Under this proposal all such income would be subtracted from Missouri income tax. Therefore, the benefit to state workers could be between \$5,578,359 (top rate 4.7%) to \$5,340,982 (top rate 4.5%). B&P notes that these numbers are included in the estimates above.

**Section 143.121.3(15) - Individual Income Tax Subtraction- Tip Income**

Officials from the **Department of Revenue (DOR)** note currently in Missouri, taxpayers are required to report all sources of income they receive and pay individual income tax if they have a tax liability after all qualifying subtractions, exemptions and deductions are applied. This proposal would expand the income that would be exempt from taxation. This proposal would allow 100% of the tips received by or paid to a tipped employee to be subtracted from the taxpayer's Missouri adjusted gross income when calculating their tax liability.

DOR notes that currently the IRS requires employers that pay an employee to report the employee's earnings in Box 1 of a W-2. Tipped income is reported along with all other wages

and salary in the same box on the form. Therefore, DOR is unable to know how much income reported comes from tips rather than other sources.

An employer must also report all allocated tips received by employees in box 8 of the W-2. Allocated tips are tips that a waitress could receive but gave to a bus boy helping to clear and serve. Allocated tips are a small percentage of the total tips received. DOR records for tax year 2023, showed 639 returns reported at least \$1,390,655 in allocated tips.

Using data from the Bureau of Labor Statistics DOR was able to identify 72,260 people holding jobs in this state that are in occupations that rely on tips. Waiters and waitresses, hairdressers, concierges, tax drivers and more. Further research into occupations found that 2.5% of people are tipped employee. Of those only 37% have income high enough to necessitate the need to file taxes. However, using the numbers from all occupations in the state and applying the same 2.5% rate DOR was able to find 71,910 that may potential have tipped income.

Using the BLS records DOR notes that of the 72,260 people in the limited occupations, only 45,524 may have enough income to file taxes and using the median salary DOR estimates they would have at least \$798,448,076 in reportable income. Using all occupations in the state, DOR assumes that the 45,303 may have \$1,123,242,582 in reportable income.

DOR assumes this proposal could result in a loss of \$798,448,076 to \$1,123,242,582 in lost revenue. DOR notes that subtractions do not reduce tax liability on a dollar-for-dollar basis but on the top tax rate applied. SB 3 adopted in 2022, has set the individual income tax top rate at 4.7% for tax year 2025 and it is expected to reduction the rate further in future fiscal years to 4.5%. DOR will show the impact of this proposal through the implementation of SB 3.

Estimated Impact by Tax Year

Tax Rate	Tax Year 2026		Tax Year 2027		Tax Year 2028	
	Low	High	Low	High	Low	High
4.70%	(\$37,527,060)	(\$52,792,401)	(\$37,527,060)	(\$52,792,401)	(\$37,527,060)	(\$52,792,401)
4.60%	(\$36,728,611)	(\$51,669,159)	(\$36,728,611)	(\$51,669,159)	(\$36,728,611)	(\$51,669,159)
4.50%			(\$35,930,163)	(\$50,545,916)	(\$35,930,163)	(\$50,545,916)

DOR notes this bill would become effective on August 28, 2025, but this subtraction is for tax year 2026 (January 1, 2026). This proposal does say that the employer would no longer be required to remit withholding tax on these employees after January 1, 2026, so DOR expects an immediate impact to revenue starting in tax year 2026.

DOR notes that this proposal would require DOR to modify the MO-1040 & MO-A (\$2,200 each), the department's website and its individual income tax computer program (\$7,327).

Officials from the **Office of Administration - Budget and Planning (B&P)** note beginning with tax year 2026, this proposal would exempt all income earned as tips.

Based on research published by Yale University, approximately 2.5% of the workforce is in an occupation that is customarily tipped. In addition, of those workers around 37% do not make enough money to have an income tax liability.

Based on data published by the U.S. Bureau of Labor Statistics – Occupational Employment and Wage Statistics, B&P estimates that there are around 71,910 to 72,260 tipped workers in Missouri, of which approximately 45,303 to 45,524 earn enough to have taxable income.

Based on additional data published by the BLS, the median income related to a tipping profession was between \$32,781 and \$40,080. Therefore, B&P estimates that this proposal could impact between \$1.45 billion to \$2.04 billion in income.

However, based on information published by the IRS, research indicates that only 55% of tipped income is actually reported. Therefore, this proposal could exempt \$798,448,076 to \$1,123,242,582 in income annually.

However, subtractions 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). Table 3 shows the potential impact by tax year.

Table 3: Estimated Impact by Tax Year

Tax Rate	Tax Year 2026		Tax Year 2027		Tax Year 2028	
	Low	High	Low	High	Low	High
4.70%	(\$37,527,060)	(\$52,792,401)	(\$37,527,060)	(\$52,792,401)	(\$37,527,060)	(\$52,792,401)
4.60%	(\$36,728,611)	(\$51,669,159)	(\$36,728,611)	(\$51,669,159)	(\$36,728,611)	(\$51,669,159)
4.50%			(\$35,930,163)	(\$50,545,916)	(\$35,930,163)	(\$50,545,916)

B&P notes that this proposal allows employers to stop withholding taxes immediately. Therefore, B&P estimates that this proposal could reduce TSR and GR in FY26 by \$18,364,306 to \$26,396,201. Once SB 3 (2022) has fully implemented, this proposal could reduce TSR and GR by \$35,930,163 to \$50,545,916 annually.

### **Summary**

This proposal could reduce TSR and GR by \$68,887,003 to \$199,677,963 in FY26. Once SB 3 (2022) has fully implemented, this proposal could reduce TSR and GR by \$134,778,976 to \$382,362,057 annually.

Table 4: Estimated GR Impact by Tax Year

Tax Rate	Tax Year 2026		Tax Year 2027		Tax Year 2028	
	Low	High	Low	High	Low	High
4.70%	(\$140,769,154)	(\$399,355,926)	(\$140,769,154)	(\$399,355,926)	(\$140,769,154)	(\$399,355,926)
4.60%	(\$137,774,065)	(\$390,858,992)	(\$137,774,065)	(\$390,858,992)	(\$137,774,065)	(\$390,858,992)
4.50%			(\$134,778,976)	(\$382,362,057)	(\$134,778,976)	(\$382,362,057)

Responses regarding the proposed legislation as a whole

Given the number of returns which might be affected, **Oversight** will show DOR's abovementioned 1 FTE for purposes of this fiscal note. If multiple bills pass which require additional staffing and duties at substantial costs, DOR could request funding through the appropriation process.

**Oversight** notes both DOR and B&P's estimates include data from DOR and B&P's internal Income Tax Model. Oversight will utilize B&P's estimated impact for this proposal.

**Oversight** notes for the purpose of the fiscal note, Oversight assumes a top income tax rate of 4.7% in tax year 2025 (FY 2026) and future income tax rate reductions from SB 3 (2022) will trigger consecutively (4.6% in FY 2027 and 4.5% in FY 2028+).

<u>FISCAL IMPACT – State Government</u>	FY 2026 (10 Mo.)	FY 2027	FY 2028
<b>GENERAL REVENUE</b>			
<u>Costs - §143.121</u>			
Personal Service	(\$30,850)	(\$37,760)	(\$38,516)
Fringe Benefits	(\$25,525)	(\$30,926)	(\$31,229)
Expense & Equipment	(\$31,947)	\$0	\$0
<u>Total Costs -</u>	(\$88,322)	(\$68,686)	(\$69,745)
FTE Change	1 FTE	1 FTE	1 FTE
<u>Revenue Loss - §143.121.3(14) - Individual Income Tax Subtraction - Overtime Income</u>	(\$101,045,454 to \$339,189,833)	(\$98,848,813 to \$331,816,141)	(\$98,848,813 to \$331,816,141)
<u>Revenue Loss - §143.121.3(15) - Individual Income Tax Subtraction - Tip Income</u>	(\$36,728,611 to \$51,669,159)	(\$35,930,163 to \$50,545,916)	(\$35,930,163 to \$50,545,916)

<u>FISCAL IMPACT – State Government</u>	FY 2026 (10 Mo.)	FY 2027	FY 2028
<b>ESTIMATED NET EFFECT ON GENERAL REVENUE</b>	<b><u>(\$137,862,387 to \$390,947,314)</u></b>	<b><u>(\$134,847,662 to \$382,430,743)</u></b>	<b><u>(\$134,848,721 to \$382,431,802)</u></b>
Estimated Net FTE Change on General Revenue	1 FTE	1 FTE	1 FTE

<u>FISCAL IMPACT – Local Government</u>	FY 2026 (10 Mo.)	FY 2027	FY 2028
	<b><u>\$0</u></b>	<b><u>\$0</u></b>	<b><u>\$0</u></b>

FISCAL IMPACT – Small Business

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

FISCAL DESCRIPTION

Beginning January 1, 2026, this bill allows taxpayers to subtract from their Federal adjusted gross income 100% of overtime compensation. Beginning January 1, 2026, this bill allows taxpayers to subtract from their Federal adjusted gross income 100% of any tips received or paid to a tipped employee engaged in an occupation that customarily and regularly receives tips.

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  
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March 30, 2025



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March 30, 2025