COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

**FISCAL NOTE**

L.R. No.: 5469-01
Bill No.: HB 1688
Subject: Taxation and Revenue - Income
Type: Original
Date: February 25, 2014

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Bill Summary: This proposal would exempt all income below the poverty line from tax.

## FISCAL SUMMARY

| ESTIMATED NET EFFECT ON GENERAL REVENUE FUND | | | |
|---|---|---|---|
| FUND AFFECTED | FY 2015 | FY 2016 | FY 2017 |
| General Revenue | $0 | ($1,062,356,200) | ($1,062,386,339) |
| | | | |
| **Total Estimated Net Effect on General Revenue Fund** | **$0** | **($1,062,356,200)** | **($1,062,386,339)** |

| ESTIMATED NET EFFECT ON OTHER STATE FUNDS | | | |
|---|---|---|---|
| FUND AFFECTED | FY 2015 | FY 2016 | FY 2017 |
| | | | |
| | | | |
| **Total Estimated Net Effect on Other State Funds** | **$0** | **$0** | **$0** |

Numbers within parentheses: ( ) indicate costs or losses.
This fiscal note contains 11 pages.

| ESTIMATED NET EFFECT ON FEDERAL FUNDS | | | |
|---|---|---|---|
| FUND AFFECTED | FY 2015 | FY 2016 | FY 2017 |
| | | | |
| | | | |
| **Total Estimated Net Effect on All Federal Funds** | **$0** | **$0** | **$0** |

| ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE) | | | |
|---|---|---|---|
| FUND AFFECTED | FY 2015 | FY 2016 | FY 2017 |
| General Revenue | 0 | 3 FTE | 3 FTE |
| | | | |
| **Total Estimated Net Effect on FTE** | **0** | **3 FTE** | **3 FTE** |

☐ Estimated Total Net Effect on All funds expected to exceed $100,000 savings or (cost).

☒ Estimated Net Effect on General Revenue Fund expected to exceed $100,000 (cost).

| ESTIMATED NET EFFECT ON LOCAL FUNDS | | | |
|---|---|---|---|
| FUND AFFECTED | FY 2015 | FY 2016 | FY 2017 |
| **Local Government** | **$0** | **$0** | **$0** |

## FISCAL ANALYSIS

ASSUMPTION

Officials from the **Office of the Secretary of State (SOS)** assume many bills considered by the General Assembly include provisions allowing or requiring agencies to submit rules and regulations to implement the act. The SOS is provided with core funding to handle a certain amount of normal activity resulting from each year's legislative session. The fiscal impact for this fiscal note to the Secretary of State's Office for Administrative Rules is less than $2,500. The SOS recognizes that this is a small amount and does not expect that additional funding would be required to meet these costs. However, we also recognize 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 our office can sustain with our core budget. Therefore, we reserve 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.

Officials from the **Office of Administration - Division of Budget and Planning (BAP)** assume this proposal would not result in any additional costs or savings to their organization.

BAP officials assume this proposal would provide that, for tax years beginning 1/1/15, the tax rate on taxable income below the poverty line would be 0%, while the tax rate for taxable income above the poverty line would be 6%.

BAP officials stated it is unclear from this proposal what is meant by the term poverty line. BAP officials used 2011 data to estimate the revenue impact of this proposal, and assumed the federal poverty guidelines for 2011 would apply, as published by the United States Department of Health and Human Services; however, the United States Census Bureau also publishes poverty thresholds which differ slightly.

Further, BAP notes that differing poverty guidelines are provided based on "family" size; BAP cannot determine how this might relate to taxpayers and their households, but the applicable guideline is likely different for each taxpayer.

ASSUMPTION (continued)

| 2011 Poverty Guidelines | |
|---|---|
| Family size | 48 Contiguous states and District of Columbia |
| 1 | $10,890 |
| 2 | $14,710 |
| 3 | $18,530 |
| 4 | $22,530 |
| 5 | $26,170 |
| 6 | $29,990 |
| 7 | $33,810 |
| 8 | $37,630 |
| Add for each additional family member | $3,820 |

BAP officials also stated it is uncertain how to apply the proposed tax rates to the proposed taxable income brackets, even if the appropriate poverty guideline could be applied to available data.

* BAP officials stated that if the full 6% rate would be applied only to any income above the poverty guideline, the impact on Total State Revenues may be similar to the estimates for HB 1269, LR 4638.

* BAP officials stated that if taxable income exceeds the guideline by any amount and the 6% rate would be applied to the filer's entire taxable income, their assumption would lead to a different estimate. It is possible Total State Revenues could increase because some taxpayers would have a higher marginal tax rate.

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ASSUMPTION (continued)

BAP officials also assume this proposal would impact the calculation under Article X, Section 18(e).

Officials from the **Department of Revenue (DOR)** assume this proposal would, beginning January 1, 2015, change Missouri individual income tax rates so that Missouri taxable income is taxed at a rate of:

| Amount of income | Tax rate |
|---|---|
| Not over the poverty line | Zero percent |
| Over the poverty line | Six percent |

Fiscal impact

DOR officials stated they assume the legislation is referring to the Federal Poverty Guidelines as depicted below for 2013-2014:

| **Household Size** | |
|---|---|
| 1 | $11,490 |
| 2 | $15,510 |
| 3 | $19,530 |
| 4 | $23,550 |
| 5 | $27,570 |
| 6 | $31,590 |
| 7 | $35,610 |
| 8 | $39,630 |
| For each additional person, add | $4,020 |

The Department assumed an average official poverty line of $23,550 for all filers and estimated that reducing the tax rate to zero on all income below the official poverty line and taxing all other income at 6 percent would result in a reduction in individual income tax revenues of $1.46 billion.

ASSUMPTION (continued)

Administrative impact

DOR officials provided the following estimate of administrative impact.

Personal Tax would require programming support for the personal income tax system, and form changes. Collections and Tax Assistance (CATA) would see additional customer contacts from the tax rate change and from notices of adjustments, and would require two additional Tax Collection Technicians I for contacts on the delinquent and non-delinquent tax lines, and one additional Revenue Processing Technician I for contacts to the field offices. Each technician would require CARES equipment and license.

DOR officials assume the Federal Poverty Guidelines would be subject to change each year so withholding tax tables would need to be updated, as well as forms and information on the DOR website.

The DOR estimate of cost to implement this proposal included three additional employees; with benefits, equipment, and expense, the DOR estimate totaled $128,070 for FY 2015, $124,065 for FY 2016, and $124,354 for FY 2017.

**Oversight** assumes the DOR estimate of expense and equipment cost for the new FTE could be overstated. If DOR is able to use existing desks, file cabinets, chairs, etc., the estimate for equipment could be reduced by roughly $6,000 per new employee.

**Oversight** assumes the additional DOR employees would be required beginning January 2016 (FY 2016) when tax returns for 2015 would be filed and will include DOR costs for six months in FY 2016. Oversight has, for fiscal note purposes only, changed the starting salary for the additional employees to correspond to the second step above minimum for comparable positions in the state's merit system pay grid. This decision reflects a study of actual starting salaries for new state employees and policy of the Oversight Subcommittee of the Joint Committee on Legislative Research. Oversight has also adjusted the DOR estimate of equipment and expense in accordance with OA budget guidelines. Finally, Oversight assumes a limited number of additional employees could be accommodated in existing office space.

ASSUMPTION (continued)

IT impact

DOR officials provided an estimate of the IT cost to implement this proposal of $13,759 based on 504 hours of programming to make changes to DOR individual tax systems.

**Oversight** assumes OA - ITSD (DOR) is provided with core funding to handle a certain amount of activity each year. Oversight assumes OA - ITSD (DOR) could absorb the costs related to this proposal. If multiple bills pass which require additional staffing and duties at substantial costs, OA - ITSD (DOR) could request funding through the appropriation process.

Officials from the **University of Missouri - Economic and Policy Analysis Research Center (EPARC)** assume that, if enacted, this legislation would exempt taxable income as currently defined up to the official federal poverty line from tax. Taxable income in excess of the official federal poverty line would be taxed at a flat rate of 6%.

EPARC officials noted the term "poverty guideline" is a simplification of the poverty thresholds used for administrative purposes – for instance, determining financial eligibility for certain federal programs; however EPARC officials used the following poverty guidelines to determine their estimate of fiscal impact.

ASSUMPTION (continued)

The official poverty guidelines 2013 published by the U.S. Department of Health and Human Services provide the following table for the 48 contiguous states and the District of Columbia:

| Number of family members | Household Poverty Guideline |
|---|---|
| 1 | $11,490 |
| 2 | $15,510 |
| 3 | $19,530 |
| 4 | $23,550 |
| 5 | $27,570 |
| 6 | $31,590 |
| 7 | $35,610 |
| 8 | $39,630 |
| Each additional person | Add $4,020 |

EPARC officials noted the baseline simulation using existing provisions and the most recent individual income tax data for 2012 indicated a Net Tax Due of $5,109.439 million.

Based on filing status and number of dependents, EPARC officials then estimated the taxable income level at which each Missouri filer would begin paying the 6% rate. When EPARC officials used the household size and poverty line for each filer from the table above, the simulation indicated a Net Tax Due of $4,047.164 million, a reduction of $1,062.275 million.

Officials from the **Joint Committee on Administrative Rules** assume this proposal would not have a fiscal impact to their organization.

ASSUMPTION (continued)

**Oversight** will use the EPARC simulation of fiscal impact in this fiscal note. Oversight notes this proposal would change Missouri income tax provisions for 2015 and assumes the fiscal impact would begin in January 2016 (FY 2016) when individual income tax returns for 2015 would be filed. Oversight is aware that some filers would reduce their estimated payments and withholding in anticipation of a tax reduction but for fiscal note purposes will include the full estimated impact of the proposed changes in the year in which tax returns would be filed. Oversight assumes the federal poverty guidelines could change from 2015 to 2016 but is not able to estimate the amount by which those guidelines could change, and will include the same estimate of fiscal impact for FY 2016.

| FISCAL IMPACT - State Government | FY 2015 (10 Mo.) | FY 2016 | FY 2017 |
|---|---|---|---|
| **GENERAL REVENUE FUND** | | | |
| | | | |
| Cost - DOR | | | |
| Individual income tax rates | | | |
| Section 143.011 | | | |
| Salaries | $0 | ($35,460) | ($71,629) |
| Benefits | $0 | ($18,086) | ($36,534) |
| Equipment and expense | $0 | ($27,654) | ($3,176) |
| Total | $0 | ($81,200) | ($111,339) |
| FTE change - DOR | 0 FTE | 3 FTE | 3 FTE |
| | | | |
| Revenue reduction - DOR | | | |
| Individual income tax rates | | | |
| Section 143.011 | $0 | ($1,062,275,000) | ($1,062,275,000) |
| | | | |
| **ESTIMATED NET EFFECT ON GENERAL REVENUE FUND** | **$0** | **($1,062,356,200)** | **($1,062,386,339)** |
| | | | |
| Estimated Net FTE Effect on General Revenue Fund | 0 FTE | 3 FTE | 3 FTE |

| FISCAL IMPACT - Local Government | FY 2015 (10 Mo.) | FY 2016 | FY 2017 |
|---|---|---|---|
| | **$0** | **$0** | **$0** |

FISCAL IMPACT - Small Business

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

FISCAL DESCRIPTION

This proposal would change the individual income tax rates to consider the poverty line.

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

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SOURCES OF INFORMATION

Office of the Secretary of State
Joint Committee on Administrative Rules
Office of Administration
Division of Budget and Planning
Department of Revenue
University of Missouri
Economic and Policy Analysis Research Center

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