

COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 4054H.02C
Bill No.: HCS for HB 1740
Subject: Taxation and Revenue - General; Employees - Employers
Type: Original
Date: February 16, 2022

Bill Summary: This proposal modifies provisions relating to earnings tax.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND			
FUND AFFECTED	FY 2023	FY 2024	FY 2025
General Revenue*	Could exceed \$362,435 to \$419,096	\$0 to Unknown	\$0 to Unknown
Total Estimated Net Effect on General Revenue	Could exceed \$362,435 to \$419,096	\$0 to Unknown	\$0 to Unknown

* A reduction in earnings tax collections (or larger earnings tax refunds), would reduce the amount of deductions used in calculating Missouri's income tax, thereby increasing state income tax collections. At a current tax rate of 5.3%, if \$4.63 million of earnings tax refunds are issued, this may equate to a positive impact to the state of over \$250,000. For FY23, \$6.92 million to \$7.99 million was used to calculate the amount of savings for the state from tax refunds.

ESTIMATED NET EFFECT ON OTHER STATE FUNDS			
FUND AFFECTED	FY 2023	FY 2024	FY 2025
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 2023	FY 2024	FY 2025
Total Estimated Net Effect on <u>All</u> Federal Funds	\$0	\$0	\$0

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)			
FUND AFFECTED	FY 2023	FY 2024	FY 2025
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 2023	FY 2024	FY 2025
Local Government*	\$0 or Less than (\$87,314,390)	\$0 or (\$20,000,000 to Unknown)	\$0 or (\$20,000,000 to Unknown)

*The fiscal impact depends upon the number of workers (taxpayers) telecommuting or working remotely. Work circumstances in future years may be very different than 2020/2021.

FISCAL ANALYSIS

ASSUMPTION

Officials from the **Office of Administration - Budget and Planning (B&P)** assume the proposal may increase Total State Revenue (TSR) by \$362,435 to \$419,096 in FY 23 and have an unknown impact to TSR in future years. This proposal will also impact the calculation under Article X, Section 18(e).

This proposal would exempt nonresident workers of Kansas City and St. Louis City from their 1% earnings tax, for the days that the nonresidents worked remotely. The proposal would begin with all tax returns filed after January 1, 2022. B&P notes that such tax returns would be for tax year 2021 earnings.

B&P further notes that the height of remote working, related to the COVID-19 pandemic, was tax year 2020. Tax returns for tax year 2020 would have been filed during calendar year 2021, and while non-resident workers have up to one year after a return is filed to apply for a refund from the City of St. Louis, this proposal requires the initial return to be filed during 2022 or later. Therefore, this proposal will only impact earnings during tax year 2021 or later.

B&P notes that currently Kansas City is already exempting nonresident remote workers from the earnings tax for the days that nonresident employee worked remotely. Therefore, B&P assumes that this proposal will not impact earnings tax revenues in Kansas City.

B&P notes that St. Louis City is not exempting nonresident income for days that the nonresident worked remotely.

B&P is unable to determine the number of working days that nonresidents work remotely; therefore, the estimates below reflect the maximum amount of revenue impacts to St. Louis City and state general revenue. Actual revenue impacts per year may vary depending on the level of actual remote work that occurs.

Based on data published by the U.S. Census Bureau 57.1% of St. Louis City residents are employed within city. Based on data previously published by MERIC (Missouri Economic Research and Information Center) approximately 5.8% of workers in St. Louis reside in Illinois. Therefore, B&P estimates that approximately 37.1% of St. Louis City workers reside within Missouri, but outside of St. Louis City.

Using data published by St. Louis City¹, B&P determined that earnings tax collections for FY20 was \$156,910,000. Therefore, B&P estimates that of the \$156,910,000 approximately \$89,595,610 comes from St. Louis City residents who work within the city, \$9,100,780 comes from Illinois residents, and \$58,213,610 comes from Missouri residents outside of St. Louis City. B&P notes that city residents would still be liable for the tax because of their residency status. Therefore, B&P estimates that this provision could reduce St. Louis City earnings tax by \$67,314,390 (\$156,910,000 total earning tax - \$89,595,610 St. Louis City residents).

B&P notes that some taxpayers claim the amount of earnings tax paid to St. Louis City in their itemized deductions. Based on information provided by DOR, B&P determined that 12% of Missouri taxpayers itemize their deductions. B&P further notes that residents outside of Missouri are not liable for Missouri income tax on the days where they worked remotely. Therefore, B&P estimates that \$6,917,558 to \$7,999,009 [(\$58,213,610 MO residents x 12%) + (\$0 to \$9,100,780 Illinois residents x 12%)] in deductions would no longer be claimed on Missouri's individual income tax returns.

However, deductions do not impact revenues on a dollar for dollar bases, but rather in proportion to the top tax rate applied. B&P notes that the top income tax rate for tax year 2022 is 5.3%, with additional reductions scheduled to occur.

B&P notes that this proposal would not become effective until August 28, 2022 after tax year 2021 returns have been filed (April 2022). Therefore, B&P will assume that this proposal will not impact state revenues until tax year 2022 returns are filed in April 2023.

Therefore, B&P assumes that this provision may reduce St. Louis City earnings tax revenue by less than \$67,314,390 in FY23. In addition, this proposal may increase general revenue by less than \$362,435 to \$419,096 (top tax rate 5.3%) in FY23.

Oversight notes the 12% itemized deduction percentage used by B&P is a rounded percentage. B&P stated to Oversight that the percentage is closer to 11.88% in the calculation of their numbers above. **Oversight** does not have information to the contrary and therefore, Oversight will reflect the estimates as provided by the B&P.

In response to a previous version, officials from the **City of St. Louis** stated the Earnings Tax is the City's single largest source of revenue amounting to over a third of the general fund budget. Total receipts in FY2020 exceeded \$175M. The proposed legislation would eliminate the Earnings Tax on nonresidents of the City who telecommute or work remotely. While there is no definitive total of the portion of the Earnings Tax this would represent, it is fair to assume that with approximately half or more of earnings tax receipts coming from non-residents, the subset of these who telecommute particularly in a year which encompassed a pandemic would be

¹ <https://www.stlouis-mo.gov/government/departments/comptroller/documents/current-comprehensive-annual-financial-report.cfm>, FY20 CAFR – Table 9, page 213

substantial. A loss of revenue of this magnitude would be a devastating blow to the City's credit and fiscal condition, and would seriously impair the City's ability to provide basic City services. The following illustration shows the order of magnitude of these Earnings tax receipts:

1/2 Earnings Tax receipts are:

- Over half the total of the FY20 general fund expenditure of the Police Department at \$167.5M

Or:

- More than the entire Fire Department budget at \$64.3M

Or about equivalent to the costs of these services:

- Corrections and Juvenile Detention: \$46.6M
- Forestry Division trimming, weeding, and debris: \$7.9M
- Park Maintenance: \$8.5M
- Street Maintenance and Repair: \$7.1M
- Street and Alley Lighting: \$9.6M
- Building Code Compliance and Permits: \$7.9M

The potential loss of revenue in the range of \$90M annually would jeopardize the City's ability to maintain basic City services.

In addition to General Revenue, there would be a similar negative impact on all TIF developments which utilized a portion of the Earnings tax receipts in its financings, an amount which totaled \$5.5M in FY20.

In response to a previous version, officials from the **City of Kansas City** assumed this proposal would have a negative fiscal impact of at least \$20 million annually.

Oversight inquired the City of Kansas City about their response and upon the receipt of this information, Oversight will review to determine if an updated fiscal note should be prepared and seek approval to publish a new fiscal note if needed.

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

In response to a previous version, officials from the **Office of the Secretary of State (SOS)** noted 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 SOS for Administrative Rules is less than \$5,000. The SOS recognizes that this is a small amount and does not expect that additional funding would be required to meet these costs. However, the 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 the office can sustain with its core budget. Therefore, the 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 proposal. If multiple bills pass which require the printing and distribution of regulations at substantial costs, the SOS could request funding through the appropriation process.

Officials from the **Department of Revenue** and the **Joint Committee on Administrative Rules** each assume the proposal will have no fiscal impact on their respective organizations. **Oversight** does not have any information to the contrary. Therefore, Oversight will reflect a zero impact in the fiscal note for these agencies.

In response to a previous version, officials from the **Department of Labor and Industrial Relations** assumed 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 for that agency.

<u>FISCAL IMPACT – State Government</u>	FY 2023 (10 Mo.)	FY 2024	FY 2025
GENERAL REVENUE			
<u>Savings</u> – calculation of deductions relating to earnings tax	Could exceed \$362,435 to \$419,096	\$0 to <u>Unknown</u>	\$0 to <u>Unknown</u>
ESTIMATED NET EFFECT ON GENERAL REVENUE	Could exceed \$362,435 to \$419,096	\$0 to <u>Unknown</u>	\$0 to <u>Unknown</u>

<u>FISCAL IMPACT – Local Government</u>	FY 2023 (10 Mo.)	FY 2024	FY 2025
LOCAL POLITICAL SUBDIVISIONS			
<u>Revenue loss</u> – potential loss in revenue from eliminating the Earnings Tax on nonresidents of St. Louis City who telecommute or work remotely	\$0 or Less than (\$67,314,390)	\$0 or (Unknown)	\$0 or (Unknown)
<u>Revenue loss</u> – potential loss in revenue from eliminating the Earnings Tax on nonresidents of Kansas City who telecommute or work remotely	\$0 or (up to \$20,000,000)	\$0 or (up to \$20,000,000)	\$0 or (up to \$20,000,000)
ESTIMATED NET EFFECT ON LOCAL POLITICAL SUBDIVISIONS	<u>\$0 or Less than (\$87,314,390)</u>	<u>\$0 or (\$20,000,000 to Unknown)</u>	<u>\$0 or (\$20,000,000 to Unknown)</u>

FISCAL IMPACT – Small Business

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

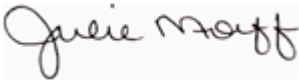
FISCAL DESCRIPTION

Currently, the law authorizes the cities of Kansas City and St. Louis to levy an earnings tax, which is imposed in part on salaries, wages, commissions, and other compensation earned by nonresidents of the city for work done or services performed or rendered in the city. For all tax returns filed on or after January 1, 2022, this bill provides that "work done or services performed or rendered in the city" will not include any work or services performed or rendered through telecommuting or otherwise performed or rendered remotely unless the location where such work is performed is located in the city. Any taxpayer denied a refund for taxes paid for such work or services not performed or rendered in the city may bring a cause of action in a court of competent jurisdiction.

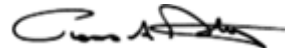
This legislation is not federally mandated, would not duplicate any other program and would not require additional capital improvements or rental space.

SOURCES OF INFORMATION

Office of Administration - Budget and Planning
City of Kansas City
City of St. Louis
Department of Labor and Industrial Relations
Department of Revenue
Joint Committee on Administrative Rules
Office of the Secretary of State



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February 16, 2022



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February 16, 2022