COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 5724-02
Bill No.: HCS for HB 2252
Subject: Taxation and Revenue - Income; Revenue Department
Type: Original
Date: March 24, 2016

Bill Summary: This proposal requires the Department of Revenue to adjust Missouri taxable income amounts used to determine income tax rates by the same amount of percentage increases in the CPI for all years between 1931 and 2017.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND				
FUND AFFECTED	FY 2017	FY 2018	FY 2019	Fully Implemented (FY 2097)
General Revenue	$0	$0	($3,394,000)	($2,645,726,000)
Total Estimated Net Effect on General Revenue	**$0**	**$0**	**($3,394,000)**	**($2,645,726,000)**

ESTIMATED NET EFFECT ON OTHER STATE FUNDS				
FUND AFFECTED	FY 2017	FY 2018	FY 2019	Fully Implemented (FY 2097)
Total Estimated Net Effect on Other State Funds	**$0**	**$0**	**$0**	**$0**

Numbers within parentheses: ( ) indicate costs or losses. This fiscal note contains 7 pages.

ESTIMATED NET EFFECT ON FEDERAL FUNDS				
FUND AFFECTED	FY 2017	FY 2018	FY 2019	Fully Implemented (FY 2097)
Total Estimated Net Effect on All Federal Funds	**$0**	**$0**	**$0**	**$0**

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)				
FUND AFFECTED	FY 2017	FY 2018	FY 2019	Fully Implemented (FY 2097)
Total Estimated Net Effect on FTE	**0**	**0**	**0**	**0**

☒ Estimated Net Effect (expenditures or reduced revenues) expected to exceed $100,000 in any of the three fiscal years after implementation of the act.

ESTIMATED NET EFFECT ON LOCAL FUNDS				
FUND AFFECTED	FY 2017	FY 2018	FY 2019	Fully Implemented (FY 2097)
Local Government	**$0**	**$0**	**$0**	**$0**

FISCAL ANALYSIS

ASSUMPTION

Beginning with 2018, this proposal would require the Department of Revenue to make annual adjustments to the individual income tax rate brackets based on the change in the Consumer Price Index for All Urban Consumers.

The first adjustment, for 2018, would be based on the inflation increase in 2015. For each subsequent taxable year, the adjustment would be based on the inflation increase in the next immediately preceding year that has not been previously used in an adjustment under this proposal. If there was no inflation increase in a particular year, the adjustment would be based on the inflation increase in the next immediately preceding year having an inflation increase. The adjustments would be required until each inflation increase in calendar years 1931 to 2015 has been applied to the tax rate tables.

The proposal would also retain the current annual tax rate bracket adjustment requirements based on the percent increase in inflation.

Officials from the **Office of Administration - Division of Budget and Planning (B&P)** assume this proposal would reduce Total State Revenues by $1,839.8 million per year when it is fully implemented. BAP officials also assume this proposal would impact the calculation required under Article X, Section 18(e) of the state constitution.

B&P officials note this proposal would require the individual income tax brackets to be adjusted for inflation from 1931 through 2017, in addition to the inflation adjustments already scheduled to occur under current law. The proposed inflation adjustment would use the Consumer Price Index for all Urban Consumers and would require the tax rate brackets to be adjusted for previous years' inflation. The proposal and current law would combine to require 2017 to be adjusted for 2016 inflation; beginning with 2018 the tax rate brackets would be adjusted for inflation in 2017 and 1934. For 2019 the tax rate brackets would be adjusted for inflation in 2018 and 1935.

This proposed additional adjustment would be applied for all years from 1931 - 2017 that had positive inflation. In the event that a year did not have positive inflation, it would be skipped and the inflation rate for the next preceding year that had inflation would be used for the second inflation adjustment

ASSUMPTION (continued)

B&P officials noted there were seven years of negative CPI growth in the period between 1931 and 2015; therefore, the secondary inflation adjustment would occur every year from Tax Year 2018 to Tax Year 2096. BAP officials provided a chart showing their estimate of TSR impact for the first five years of implementation, using the most currently available Tax Year 2013 income tax data, and the estimated impact once this proposal is fully implemented.

Oversight assumes the proposal would include inflation from 1931 through 2015 (inclusive); therefore, there would be a total of (2015-1930) = 85 years of changes in the Consumer Price Index. Subtracting seven years in which there was no or negative inflation would leave (85-7) = 78 years inflation to be applied to the tax rate bracket adjustments under this proposal. The last adjustment required under this proposal would be for 2095 individual income taxes for which tax returns would be filed in FY 2096.

B&P officials provided a detailed calculation of the revenue reduction estimated to result from this proposal as well as the following chart of estimated revenue reductions, in millions of dollars:

Fiscal year	Revenue reduction
2018	$17.4
2019	$36.4
2020	$41.5
2021	$62.9
2022	$69.7
2094	$1,839.8

B&P officials noted their numbers are based upon Tax Year 2013 data and are not modified for normal inflationary growth in revenue, and the actual reduction in future years would likely be greater and may vary due to other impacts from SB 509 (2014).

Officials from the **Department of Revenue (DOR)** assume this proposal would adjust the income tax brackets based upon the historical increase in the cost of living from 1931 to 2015 as measured by the Consumer Price Index for All Urban Consumers for the United States. DOR estimates a negative impact to Total State Revenue of $1.84 billion when fully implemented.

ASSUMPTION (continued)

For tax years beginning January 1, 2018, the DOR would be required to make an additional adjustment to the income tax rate brackets according to the percent increase in inflation for the one-year period beginning January 1, 2015. For tax years beginning after January 1, 2019, the legislation would require the DOR to make additional annual adjustments until each historical inflation increase from calendar years 1931 to 2015 has been applied to the tax rate brackets. These adjustments would be in addition to the adjustments currently required.

DOR officials stated they determined the historical average annual rate of inflation from 1931 to 2016 and combined it with an estimated average rate of future inflation of 2.1 percent to estimate the change to the tax brackets for this proposal. Using tax year 2013 data, the DOR estimated that Total State Revenue could be reduced by as much as $1.84 billion per year when fully implemented.

Officials from the **University of Missouri - Economic and Policy Analysis Research Center (EPARC)** assume this proposal would, if enacted, increase the size of the taxable income classes as they apply to the Missouri personal income tax table.

An initial adjustment in 2018 would increase the size of the tax brackets by the same percentage as the inflation rate evident in the CPI from the calendar year 2015. Subsequent years' adjustments would increase the size of the tax brackets by the same percent as the inflation rate evident in the CPI from calendar years preceding backward from 2015. Further, the proposal stated "When there was no inflation increase in the next immediate preceding year (counting backward from 2015), the director shall disregard such year and apply the percentage of inflation increase in the next immediately preceding year having an inflation increase to the next required annual adjustment."

EPARC officials reported a baseline simulation using the most recent data on individual income tax for Missouri for 2014 and the current tax rate table, and stated that estimated Net Tax Due would be $5,574.541 million. A second simulation using the same data and the adjusted rate table provided an estimated Net Tax Due of $5,571.147 million, a reduction in Net Tax Due of $3.394 million from the baseline for calendar year 2018. For the following year, EPARC officials estimate a revenue reduction of $12.620 million.

EPARC officials note the current tax brackets of $1,000 will be replaced by tax brackets of $15,593 each. As a result, the current highest marginal rate of 6% is reached on taxable income in excess of $9,000, whereas under a fully implemented change, the top marginal rate of 6% is reached on taxable income in excess of $140,339. The fully implemented effect of the proposal would result in General Revenue reduction of $2,645.726 million in the final year of implementation.

ASSUMPTION (continued)

Oversight will use this EPARC estimate of revenue reduction for the fully implemented impact of this proposal.

Officials at the **Joint Committee on Administrative Rules** assume there is no fiscal impact from this proposal.

Officials from the **Office of the Secretary of State (SOS)** state 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 $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, 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 the 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.

FISCAL IMPACT - State Government	FY 2017 (10 Mo.)	FY 2018	FY 2019	Fully Implemented (FY 2097)
GENERAL REVENUE				
Revenue reduction- Tax rate bracket adjustments	$0	$0	($3,394,000)	($2,645,726,000)
ESTIMATED NET EFFECT TO GENERAL REVENUE	**$0**	**$0**	**($3,394,000)**	**($2,645,726,000)**

FISCAL IMPACT - Local Government	FY 2017 (10 Mo.)	FY 2018	FY 2019	Fully Implemented (FY 2097)
	$0	**$0**	**$0**	**$0**

FISCAL IMPACT - Small Business

This proposal would not have a direct impact to small businesses but would reduce income taxes to owners of small businesses.

FISCAL DESCRIPTION

Beginning January 1, 2018, this bill requires the Department of Revenue to adjust Missouri taxable income amounts used to determine income tax brackets by the same amount of percentage increases in inflation for all years between 1931 and 2015.

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

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