

COMMITTEE ON LEGISLATIVE RESEARCH  
OVERSIGHT DIVISION

**FISCAL NOTE**

L.R. No.: 1360-01  
Bill No.: SB 260  
Subject: Taxation and Revenue - Income  
Type: Original  
Date: March 8, 2019

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Bill Summary: This proposal increases the amount of the personal income tax cut and the business income deduction in current law.

**FISCAL SUMMARY**

<b>ESTIMATED NET EFFECT ON GENERAL REVENUE FUND</b>				
FUND AFFECTED	FY 2020	FY 2021	FY 2022	Fully Implemented (FY 2024)
General Revenue	Unknown or (Unknown) to (\$46,100,000)	Unknown or (Unknown) to (\$154,800,000)	Unknown or (Unknown) to (\$270,100,000)	Unknown or (Unknown) to (\$556,600,000)
<b>Total Estimated Net Effect on General Revenue</b>	<b>Unknown or (Unknown) to (\$46,100,000)</b>	<b>Unknown or (Unknown) to (\$154,800,000)</b>	<b>Unknown or (Unknown) to (\$270,100,000)</b>	<b>Unknown or (Unknown) to (\$556,600,000)</b>

**\* Oversight assumes a positive unknown to negative unknown for revenue estimates until we are able to estimate revenue or verify the data and models provided. Oversight will also reflect B&P's revenue estimates for the changes to the tax rates.**

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

<b>ESTIMATED NET EFFECT ON OTHER STATE FUNDS</b>				
<b>FUND AFFECTED</b>	<b>FY 2020</b>	<b>FY 2021</b>	<b>FY 2022</b>	<b>Fully Implemented (FY 2024)</b>
<b>Total Estimated Net Effect on <u>Other</u> State Funds</b>	<b>\$0</b>	<b>\$0</b>	<b>\$0</b>	<b>\$0</b>

<b>ESTIMATED NET EFFECT ON FEDERAL FUNDS</b>				
<b>FUND AFFECTED</b>	<b>FY 2020</b>	<b>FY 2021</b>	<b>FY 2022</b>	<b>Fully Implemented (FY 2024)</b>
<b>Total Estimated Net Effect on <u>All</u> Federal Funds</b>	<b>\$0</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 2020</b>	<b>FY 2021</b>	<b>FY 2022</b>	<b>Fully Implemented (FY 2024)</b>
<b>Total Estimated Net Effect on FTE</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>

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

<b>ESTIMATED NET EFFECT ON LOCAL FUNDS</b>				
<b>FUND AFFECTED</b>	<b>FY 2020</b>	<b>FY 2021</b>	<b>FY 2022</b>	<b>Fully Implemented (FY 2024)</b>
<b>Local Government</b>	<b>\$0</b>	<b>\$0</b>	<b>\$0</b>	<b>\$0</b>

## FISCAL ANALYSIS

### ASSUMPTION

**Oversight** notes the current projected Individual Income Tax Rate is calculated with SB 509 (2014) and HB 2540 (2018) reductions as follows:

TY 2018 it was 5.9% (.1% reduction from SB 509)

TY 2019 it is 5.4% (.1% reduction from SB 509 + .4% reduction from HB 2540)

TY 2020 will be 5.3% (.1% reduction from SB 509)

TY 2021 will be 5.2% (.1% reduction from SB 509)

TY 2022 will be 5.1% (last .1% reduction from SB 509)

Officials at the **Office of Administration Division of Budget and Planning (B&P)** assume §143.011.2 would end the current rate reductions, created under SB 509 (2014), after two reductions. B&P notes that as of tax year 2019, two reductions have now occurred.

Section 143.011.4 would create additional top rate reductions beginning tax year 2020. The top rate of tax may be reduced by 0.2% each year that net general revenue collected in the previous fiscal year exceeds the highest amount of net general revenue collected in any of the three previous fiscal years by at least \$150 million. The aggregate amount of reductions shall not exceed 0.8%. Table 1 shows the tax rate changes under this proposal.

Table 1: Tax Rates

Tax Year	Current Law	Proposal*
2019	5.4%	5.4%
2020	5.3%	5.2%
2021	5.2%	5.0%
2022	5.1%	4.8%
2023	5.1%	4.6%

\*Assumes growth triggers occur in consecutive years

Section 143.022.4 would increase the amount of pass-through business income exempt from individual income tax from 5% increments to 10% increments, beginning with tax year 2020. B&P notes that the current pass-through business exemption was 5% in tax year 2018 and has increased to 10% for tax year 2019. Table 2 shows the pass-through business exemption under this proposal.

ASSUMPTION (continued)

Table 2: Pass-through Business Exemption

Tax Year	Current Law	Proposal*
2019	10%	10%
2020	15%	20%
2021	20%	30%
2022	20%	40%
2023	20%	50%

\*Assumes growth triggers occur in consecutive years

For the purpose of this fiscal note, B&P will assume that the income tax rate reductions and business income exemptions scheduled to occur under current law and under this proposal happen in consecutive years. Based on tax year 2016 data, the most recent complete tax year available, B&P estimates that this proposal will decrease Total State Revenue and General Revenue by \$46.1 million in FY 2020. Once fully implemented, in FY 2024, B&P estimates that this proposal will decrease Total State Revenue and General Revenue by \$556.6 million annually. The following tables show B&P's estimated impacts by tax year and fiscal year.

Table 3: Estimated Impact by Tax Year

Tax Year	GR Loss
2020	(\$109.7)
2021	(\$217.2)
2022	(\$343.0)
2023	(\$556.6)

\*Assumes growth triggers occur in consecutive years

Table 4: Estimated Impact by Fiscal Year

Fiscal Year	GR Loss
2020	(\$46.1)
2021	(\$154.8)
2022	(\$270.1)
2023	(\$432.7)
2024	(\$556.6)

\*Assumes growth triggers occur in consecutive years

**Oversight** notes that B&P uses a 42% in first fiscal year and 58% split in the second year to convert the income tax numbers from tax year to fiscal year.

ASSUMPTION (continued)

**Oversight** will use the estimates provided by B&P for the fiscal note.

Officials at the **Department of Revenue (DOR)** assume the Department used its internal Income Tax Model that contains confidential taxpayer data to create the fiscal impact. The Department believes that the tax rates, as proposed, could become as follows:

<b>Tax Rates</b>	
<b>Tax Year</b>	<b>Rate</b>
2018	5.90%
2019	5.40%
2020	5.20%
2021	5.00%
2022	4.80%
2023	4.60%
2024	4.60%

The business income subtraction percent, as proposed, was analyzed for this bill as follows:

<b>Business Income Subtraction Percent</b>	
<b>Tax Year</b>	<b>Percentage</b>
2018	5%
2019	10%
2020	20%
2021	30%
2022	40%
2023	50%
2024	50%

ASSUMPTION (continued)

Impact to Total State Revenues

<b>Fiscal Year</b>	<b>Impact</b>
<b>FY 20</b>	\$0.0
<b>FY 21</b>	(\$46,807,153.30)
<b>FY 22</b>	(\$157,290,075.90)
<b>FY 23</b>	(\$274,911,890.50)
<b>FY 24</b>	(\$445,150,465.20)
<b>FY 25</b>	(\$576,665,757.00)

**Oversight** currently does not have the data or resources available to produce independent revenue projections, therefore Oversight uses the same assumptions for revenue growth as the FY 2020 Consensus Revenue Estimate (CRE) for revenue growth in all future years. The CRE assumes an increase in net general revenue collections of \$192.6 million for FY 2020.

**Oversight** notes pursuant to §143.011 - §143.022 (SBs 509 & 496 2014) if the previous fiscal year's net general revenue collections exceed the highest net general revenue collections of the three previous fiscal years by at least \$150 million, then there will be a reduction in the individual income tax rate by one-tenth of a percent and a reduction for individual income tax filers of 5% of "business income." These reductions will reduce net General Revenue collections by an estimated \$160.0 million annually. Oversight notes the proposed legislation may impact future net revenue collections and could impact future triggering of the rate reductions required under §143.011 - §143.022.

**Oversight** notes that it **does not currently have the resources and/or access to state tax data** to produce an independent revenue estimate and is unable to verify the revenue estimates provided by B&P and DOR.

Oversight assumes a positive unknown to negative unknown for revenue estimates until we are able to estimate revenue or verify the data and models provided. Oversight will also reflect B&P's revenue estimates.

Officials at the **University of Missouri Economic & Policy Analysis Research Center (EPARC)** assume this bill increases the amount of the personal income tax cut and the business income deduction in current law. Specifically, this bill would increase the personal income tax cut by an additional 0.1%. Current law states that when a revenue threshold is met, the top personal income tax rate will be cut by one-tenth of one percent the following tax year. This bill

ASSUMPTION (continued)

would increase this cut to one-fifth of one percent. As well, this bill would increase the business income deduction by 5%. Current law states that when a revenue threshold is met, the business income deduction will be increased by 5% the following tax year. This bill would allow, when the revenue threshold is met, the business income deduction to be increased by 10% the following year.

In order to estimate the maximum impact of this bill, we will need to estimate the impact of current law on General Revenue for the tax years 2020, 2021, and 2022 as if the revenue threshold within this statute were met every year. We will then estimate the impact of the parameters of this bill independently. The maximum impact of SB 280 results from the difference between these two estimates. We will subtract the impact of current law from the estimated impact of the parameters of this bill.

Impact of Current Law:

In order to estimate the maximum impact of this bill, we will need to estimate the impact of current law on General Revenue for the tax years 2020, 2021, and 2022 as if the revenue threshold within this statute were met every year. The following table shows these estimates (dollar amounts are in millions):

Year	Top Tax Rate	Business Income Deduction	Net Tax Due	Reduction in Net General Revenue
Baseline	5.40%	10%	\$5,680.602	\$0
2020	5.30%	15%	\$5,552.643	\$127.959
2021	5.20%	20%	\$5,426.503	\$254.099
2022	5.10%	25%	\$5,302.269	\$378.333

We see in the above table the reduction in Net General Revenue should the revenue threshold be met every year and the top tax rate is reduced in 0.1% increments and the business income deduction is increased in 5% increments. In 2020, current law will reduce Net General Revenue by \$127.959 million. In 2021, current law will reduce Net General Revenue by \$254.099 million. In 2022, current law will reduce Net General Revenue by \$378.333 million.



ASSUMPTION (continued)

Impact of New Parameters:

Next we will need to estimate the impact of the parameter changes suggested by this bill independently. Again, we will assume the revenue threshold will be met every year. The following table shows these estimates (dollar amounts are in millions):

Year	Top Tax Rate	Business Income Deduction	Net Tax Due	Reduction in Net General Revenue	Additional Loss of Revenue
Baseline	5.40%	10%	\$5,680.602	\$0	\$0
2020	5.20%	20%	\$5,426.503	\$254.099	\$126.140
2021	5.00%	30%	\$5,179.144	\$501.458	\$247.359
2022	4.80%	40%	\$4,934.937	\$745.665	\$367.332

We see in the above table the reduction in Net General Revenue should the revenue threshold be met every year and the top tax rate is reduced in 0.2% increments and the business income deduction is increased in 10% increments. In 2020, these new parameters will reduce Net General Revenue by \$254.099 million. In 2021, these new parameters will reduce Net General Revenue by \$501.458 million. In 2022, these new parameters will reduce Net General Revenue by \$745.665 million.

Impact of this Proposal:

As stated before, the maximum impact of this proposal results from the difference between the impact of current law and the estimated impact of the parameters of this bill.

In 2020 we estimate the parameters of this bill will reduce revenue by \$254.099 million compared to the baseline. This is an additional loss of revenue of \$126.140 million beyond the impact estimate of current law of \$127.959 million. Therefore, in 2020 we would expect a loss in Net General Revenue of \$126.140 million due to this bill.

In 2021 we estimate the parameters of this bill will reduce revenue by \$501.458 million compared to the baseline. This is an additional loss of revenue of \$247.359 million beyond the impact estimate of current law of \$254.099 million. Therefore, in 2021 we would expect a loss in Net General Revenue of \$247.359 million due to this bill.

ASSUMPTION (continued)

In 2022 we estimate the parameters of this bill will reduce revenue by \$745.665 million compared to the baseline. This is an additional loss of revenue of \$367.332 million beyond the impact estimate of current law of \$378.333 million. Therefore, in 2022 we would expect a loss in Net General Revenue of \$367.332 million due to this bill.

Conclusion: In 2020 we would expect a loss in Net General Revenue of \$126.140 million due to this bill. In 2021 we would expect a loss in Net General Revenue of \$247.359 million due to this bill. In 2022 we would expect a loss in Net General Revenue of \$367.332 million due to this bill.

<u>FISCAL IMPACT -</u> <u>State Government</u>	FY 2020 (6 Mo.)	FY 2021	FY 2022	Fully Implemented (FY 2024)
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**GENERAL  
REVENUE**

<u>Revenue Reduction -</u> DOR §143.011 & §143.022 reduction in individual income tax rate and pass through rate	<u>(\$46,100,000)</u>	<u>(\$154,800,000)</u>	<u>(\$270,100,000)</u>	<u>(\$556,600,000)</u>
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**ESTIMATED NET  
EFFECT ON  
GENERAL  
REVENUE**

	<u>(\$46,100,000)</u>	<u>(\$154,800,000)</u>	<u>(\$270,100,000)</u>	<u>(\$556,600,000)</u>
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**\* Oversight assumes a positive unknown to negative unknown for revenue estimates until we are able to estimate revenue or verify the data and models provided. Oversight will also reflect B&P's revenue estimates for the changes to the tax rates.**

<u>FISCAL IMPACT -</u> <u>Local Government</u>	FY 2020 (6 Mo.)	FY 2021	FY 2022	Fully Implemented (FY 2024)
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<u>\$0</u>	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>
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FISCAL IMPACT - Small Business

This will impact pass-through businesses through an income subtraction and reduced tax rate.

FISCAL DESCRIPTION

Current law provides for a reduction in the top rate of income tax over a period of years from 6% to 5.5%, with each cut becoming effective if net general revenue collections meet a certain trigger. This act increases the amount in which the top rate will be reduced. Each year the trigger is met, the top rate will be reduced by 0.2% rather than 0.1%. The aggregate amount of reductions to be made under this provision shall not exceed 0.8%. (§143.011)

Currently, a business income deduction is being phased in over a period of years. Each year that a general revenue growth trigger is met, the deduction amount is increased by 5%. Once fully phased in, individual taxpayers may deduct up to 20% of their business income. This act increases the amount that may be deducted. Each year that the trigger is met, the deduction amount will be increased by 10%. Once fully phased in, individual taxpayers may deduct up to 50% of their business income. (§143.022)

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 Division of Budget and Planning  
University of Missouri Economic & Policy Analysis Research Center



Kyle Rieman  
Director  
March 8, 2019

Ross Strobe  
Assistant Director  
March 8, 2019