

COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 3823-02
Bill No.: SCS for SB 583
Subject: Taxation and Revenue - Income; Teachers
Type: Original
Date: February 20, 2020

Bill Summary: This proposal allows for an income tax deduction for educator expenses.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND				
FUND AFFECTED	FY 2021	FY 2022	FY 2023	Fully Implemented (FY 2024)
General Revenue	\$0	(\$1,092,201) to (\$2,077,628)	(\$1,059,740) to (\$2,026,574)	(\$1,042,062) to (\$1,990,303)
Total Estimated Net Effect on General Revenue	\$0	(\$1,092,201) to (\$2,077,628)	(\$1,059,740) to (\$2,026,574)	(\$1,042,062) to (\$1,990,303)

ESTIMATED NET EFFECT ON OTHER STATE FUNDS				
FUND AFFECTED	FY 2021	FY 2022	FY 2023	Fully Implemented (FY 2024)
Total Estimated Net Effect on <u>Other</u> State Funds	\$0	\$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 2021	FY 2022	FY 2023	Fully Implemented (FY 2024)
Total Estimated Net Effect on <u>All</u> Federal Funds	\$0	\$0	\$0	\$0

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)				
FUND AFFECTED	FY 2021	FY 2022	FY 2023	Fully Implemented (FY 2024)
General Revenue	0 FTE	2 FTE	2 FTE	2 FTE
Total Estimated Net Effect on FTE	0 FTE	2 FTE	2 FTE	2 FTE

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 2021	FY 2022	FY 2023	Fully Implemented (FY 2024)
Local Government	\$0	\$0	\$0	\$0

FISCAL ANALYSIS

ASSUMPTION

Officials from the **Office of Administration - Budget & Planning Division (B&P)** state Section 143.121.3(12) creates a tax deduction of up to \$500 for qualifying educator expenses beginning in Tax Year 2021. The deduction would only be granted for educators and expenses that qualify for the current federal tax deduction or for teachers in an early childhood education program. B&P notes that while the deduction will become available in Tax Year 2021, the impact to General Revenue (GR) and Total State Revenue (TSR) will not occur until taxpayers file their annual return in Fiscal Year 2022.

In Tax Year 2017, the most recent complete tax year data available, there were 66,430 tax filers that claimed the federal tax deduction for a total claim amount of \$17 million, for an average claim amount of approximately \$257.

In addition, based on data published by the United States Bureau of Labor Statistics, there are approximately 5,860 preschool teachers in Missouri. B&P notes that preschool teachers do not qualify for the federal deduction. However, for the purpose of this fiscal note B&P will assume that they will have similar deduction patterns as teachers that qualify for the federal deduction.

For the purpose of this fiscal note B&P will show a range in potential revenue loss between the average of \$257 federal deduction actually claimed in Tax Year 2017 and the cap of \$500 set forth in this proposal. 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 509 (2014).

Tax Year	Current Law	TY21*	TY22*	TY23*
Tax Rate	5.40%	5.30%	5.20%	5.10%
Low Estimate	\$1,001,624	\$983,075	\$964,527	\$945,978
High Estimate	\$1,951,830	\$1,915,685	\$1,879,540	\$1,843,395

Therefore, B&P estimates that this proposal could reduce TSR and GR by \$1,001,624 to \$1,951,830 (top tax rate 5.4%) or by \$983,075 to \$1,915,685 (top tax rate 5.3%) in Fiscal Year 2022. Once SB 509 (2014) has fully implemented, this proposal could reduce TSR and GR by \$945,978 to \$1,843,395 annually.

ASSUMPTION (continued)

Oversight notes B&P assumes this proposed legislation could reduce GR and TSR by \$945,978 to \$1,843,395 when SB 509 (2014) has been fully implemented. For purposes of this fiscal note, Oversight will assume the tax rate reductions set forth in SB 509 (2014) will occur each consecutive tax year until fully implemented in Tax Year 2023.

Officials from the **Missouri Department of Revenue (DOR)** state this proposal states for all tax years beginning on or after January 1, 2021, one hundred percent of all unreimbursed educator expenses incurred by an eligible educator during the taxable year, not to exceed five hundred dollars (\$500) is eligible to be deducted from a taxpayer's Missouri Adjusted Gross Income. An eligible educator is defined as one who qualifies under 26 U.S.C. Section 62, and teachers in an early childhood education program.

DOR used IRS 2017 data for determining those who qualify under 26 U.S.C. Section 62:

Number of Filers: 66,430
 Amount: \$17,045,000
 Average Claimed: \$257

This proposal allows for a \$500 Missouri deduction while the current average amount claimed on federal tax returns is approximately \$257. Using the 66,430 number of federal filers, DOR calculated a high/low range showing the potential revenue impact if all individuals claimed at the \$257 current average amount versus all individuals claiming the proposed \$500 deduction. DOR notes that this is a deduction and therefore is not a dollar for dollar loss. DOR notes that SB 509 (2014), which is assumed to trigger a tax rate reduction each year, would additionally impact the estimate.

Tax Year	Current Law	TY21*	TY22*	TY23*
Tax Rate	5.40%	5.30%	5.20%	5.10%
Low Estimate \$257	\$921,916	\$904,843	\$887,771	\$870,698
High Estimate \$500	\$1,793,610	\$1,760,395	\$1,727,180	\$1,693,965

*assumes each SB 509 (2014) trigger is reached

This proposal allows a teacher in an early childhood education program to claim the deduction. DOR contacted the Department of Elementary and Secondary Education to determine how many additional persons would qualify as a teacher in an early childhood education program and was provided the following information.

ASSUMPTION (continued)

Missouri	Child Care Workers	Preschool Teachers, Excl. Special Ed	Preschool Teachers, Special Ed	Preschool/Child Care Center Directors	All ECE Employees
	12,890	5,050	310	630	18,880

DOR will assume the 310 preschool special education teachers and the 5,050 preschool teachers (5,360 total) would also be eligible for this tax deduction. DOR will show these teachers at the low rate of \$257 as well as the \$500 deduction established under this proposal.

Tax Year	Current Law	TY21*	TY22*	TY23*
Tax Rate	5.40%	5.30%	5.20%	5.10%
Low Estimate \$257	\$74,386	\$73,009	\$71,631	\$70,254
High Estimate \$500	\$144,720	\$142,040	\$139,360	\$136,680

DOR notes this proposal begin January 1, 2021 and the tax returns claiming the deduction would be filed starting in Fiscal Year 2022. This is estimated to be a loss to GR.

Fiscal Year	FY 2021*	FY 2022*	FY 2023*
Tax Rate	5.30%	5.20%	5.10%
Low Estimate	\$0	\$977,852	\$959,402
High Estimate	\$0	\$1,902,435	\$1,866,540

Oversight notes DOR assumes GR and TSR could be reduced by \$977,852 to \$1,902,435 in Fiscal Year 2022 and \$940,952 to \$1,830,645 when SB 509 (2014) is fully implemented. Oversight notes DOR assumes the individual income tax rate reductions pursuant to SB 509 (2014) will occur in consecutive tax years.

DOR states one (1) Revenue Processing Technician I is required for every 14,700 errors, one (1) Revenue Processing Technician I is required for every 5,700 pieces of correspondence and one (1) part-time employee is required for the new line item on Form MO-1040 (and all other forms deemed necessary).

ASSUMPTION (continued)

Oversight assumes DOR will need the requested FTE(s) based on the number of taxpayers claiming the educator expense(s) deduction at the federal level. For purposes of this fiscal note, Oversight will show the FTE cost to DOR beginning in Fiscal Year 2022. Oversight notes this would allow for 6 months before tax returns claiming the deduction proposed in this legislation would be filed. Furthermore, Oversight has adjusted the cost, as reported by DOR, to remove the fringe benefits DOR calculated for the Temporary Tax Employee.

Officials from the **University of Missouri’s Economic & Policy Analysis Research Center (EPARC)** state this proposal would create a tax deduction for educator expenses. Specifically, “for all tax years beginning on or after January 1, 2021, one hundred percent of all unreimbursed educator expenses incurred by an eligible educator during the taxable year, not to exceed \$500.”

Within EPARC’s simulation EPARC applied filers’ current federal educator expense deduction to their Missouri filing. EPARC used this prior estimation as the minimum impact estimate. To review, Table 1 shows the Baseline of EPARC’s analysis where Net Tax Due equals \$5,680.602 million. Table 2 shows the impact of enacting the aforementioned deduction. Table 2 shows Net Tax Due equal to \$5,679.802 million. This is a decrease of \$800,000 in Net Tax Due. Therefore, EPARC estimates, at minimum, the impact of this tax deduction will reduce Net General Revenue by \$800,000 in Fiscal Year 2022 and beyond.

Since EPARC is unable to identify early childhood educators within the simulation, EPARC must rely on aggregate data to calculate their additional impact. EPARC’s data indicates there are approximately 68,150 K - 12 teachers in Missouri, where 62,560 used the federal deduction for educator expenses. This is about 92% of all teachers. Within EPARC’s tax data, the aggregate total of expenses for these teachers sums to \$16,130,423 with an average of \$257.84. EPARC’s data indicates there are 5,510 preschool teachers in Missouri with an average salary of \$30,440, compared to \$52,697 for their K-12 contemporaries. In the following table, Table 1, EPARC uses these statistics to estimate the impact this deduction will have on Missouri revenue.

Table 1 - Best Approximation

Grade Level	Average Salary	Teachers Utilizing Deduction	Average Deduction	Aggregate Deductions	Tax Rate	Revenue Reduction
K - 12	\$52,697	62,560	\$258	\$16,130,423	5.4%	\$871,043
Preschool	\$30,440	5,058	\$143	\$691,540	5.4%	\$37,343

Adding the K - 12 and Preschool estimates, EPARC arrived at a \$908,386 reduction in Net General Revenue in Fiscal Year 2022 and beyond.

ASSUMPTION (continued)

EPARC provided the maximum impact estimate should the rate of utilization or average deductions increase. In Table 2, EPARC estimates the maximum potential impact.

Table 2 - Maximum Impact Approximation

Grade Level	Teachers Utilizing Deduction	Average Deduction	Aggregate Deductions	Tax Rate	Revenue Reduction
K - 12	68,150	\$500	\$34,075,000	5.4%	\$1,840,050
Preschool	5,510	\$500	\$2,755,000	5.4%	\$148,770

EPARC estimates the maximum reduction in Net General Revenue to be \$1,988,820 in Fiscal Year 2022.

Oversight notes EPARC estimates this proposed legislation could reduce GR by \$908,386 to \$1,988,820 beginning in Fiscal Year 2022. Oversight notes EPARC's estimate does not take into consideration the potential of a individual income tax rate reduction equal to one-tenth of one percent (0.1%) in Tax Year 2021.

Oversight notes that Section 143.121.3(12) establishes a deduction in an amount equal to the lesser of one hundred percent of unreimbursed educator expenses or \$500 of unreimbursed educator expenses.

Oversight notes the Internal Revenue Service (IRS) publishes Individual Income Tax Data, by state, and by size of adjusted gross income. Based on the information reported, there were approximately 66,430 individuals who filed a federal tax return with a Missouri address claiming educator expenses for Tax Year 2017. The amount of educator expenses claimed for Tax Year 2017 totaled \$17,045,000. Therefore, Oversight estimates the average amount of educator expenses claimed per filer amounts to \$257 ($\$17,045,000 / 66,430$).

Oversight also notes the Missouri Department of Elementary and Secondary Education (DESE) publishes data reporting the number of teacher FTE equivalents per school district on their website. Per the 2017 information published, there were approximately 68,726 teacher FTE reported throughout Missouri school districts.

Oversight assumes the information published by the IRS is specific to filers who file with a Missouri address. In addition, the IRS data would not capture and report information for any individual with a Missouri address that may qualify for this deduction but did not file a federal tax return. In addition, the information published by the IRS does not include teachers of any early childhood education program, as they do not qualify for the federal deduction.

ASSUMPTION (continued)

Therefore, Oversight will provide estimates using the number of teacher FTE reported by DESE (68,726) and the number of teachers of early childhood education programs used by DOR, provided by DESE (5,360) [total of 74,086].

Oversight estimates the average amount of educator expenses claimed by each individual on Federal Income Tax returns for Tax Year 2017 to equal \$257. Based on the aforementioned data, if each teacher FTE and teacher of an early childhood education program were to qualify for and claim the deduction equal to \$257, then the total amount of the deduction is estimated to be \$19,040,102 (74,086 x \$257).

Oversight notes the maximum deduction pursuant to this proposed legislation is \$500. Based on the aforementioned data, if each teacher FTE and teacher of an early childhood education program were to qualify for and claim the maximum \$500 deduction, the total amount of the deduction is estimated to be \$37,043,000 (74,086 x \$500).

The estimated amount of the total deduction does not reduce state revenues on a dollar-for-dollar basis; the total estimated deduction must be multiplied by the (top) individual income tax rate applicable for each year to produce true dollar estimates of the reduction in GR.

Oversight notes the following applicable tax rates, per tax year:

Tax Year	Top Ind. Income Tax Rate
TY 19	5.40%
TY 20	5.40%
TY 21	5.3%*
TY 22	5.2%*
TY 23	5.1%*

*Assumes the triggers pursuant to SB 509 (2014) are reached each applicable year for a .1% reduction in the top individual income tax rate.

Oversight notes this proposed legislation would allow “eligible educators” to claim the deduction proposed in this legislation beginning in Tax Year 2021. Eligible educators would not file Tax Year 2021 return(s) claiming the proposed deduction until after January 1, 2022, or Fiscal Year 2022, which would be the first year in which revenue reductions applicable to this proposed legislation could be recognized.

Oversight will assume the tax rate changes allowable pursuant to SB 509 (2014) will occur for Tax Year(s) 2021, 2022, and 2023.

ASSUMPTION (continued)

Oversight estimates the range (Low and High) of the fiscal impact (revenue reduction) beginning with the average educator expenses calculated from the Tax Year 2017 IRS data (\$257 per claimant) and ending with the maximum (\$500 per claimant) allowable, for each fiscal year until fully implemented.

Oversight estimates the following impact fiscal impact (range) to TSR and GR, pursuant to this proposed legislation:

Impact General Revenue		
Fiscal Year	Low	High
FY 2022	(\$1,009,125)	(\$1,963,279)
FY 2023	(\$990,085)	(\$1,926,236)
FY 2024	(\$971,045)	(\$1,889,193)

*Assumes the triggers pursuant to SB 509 (2014) are reached each applicable year for a .1% reduction in the top individual income tax rate.

For purposes of this fiscal note, Oversight will show the revenue impacts assuming the triggers in SB 509 (2014) have been reached resulting in a reduction of the top individual income tax rate by one tenth of one percent (0.1%).

Oversight will provide a fiscal impact including a range with a “Low” and a “High” estimate. For purposes of this fiscal note, Oversight will report the “Low” range using estimates provided by DOR and the “High” estimates using estimates calculated by Oversight.

<u>FISCAL IMPACT -</u> <u>State Government</u>	FY 2021 (10 Mo.)	FY 2022	FY 2023	Fully Implemented (FY 2024)
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**GENERAL
REVENUE FUND**

<u>Revenue Reduction</u> (Section 143.121.3) - Tax deduction for eligible educator expenses up to \$500	\$0	(\$977,852) to (\$1,963,279)	(\$959,402) to (\$1,926,236)	(\$940,952) to (\$1,889,193)
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<u>Cost - DOR (Section</u> <u>143.121.3.12)</u>				
Personal Service	\$0	(\$57,453)	(\$58,027)	(\$58,607)
Fringe Benefits	\$0	(\$42,120)	(\$42,311)	(\$42,503)
Equipment and Expense	\$0	(\$14,776)	\$0	\$0
<u>Total Cost - DOR</u>	<u>\$0</u>	<u>(\$114,349)</u>	<u>(\$100,338)</u>	<u>(\$101,110)</u>
FTE Change - DOR	0 FTE	2 FTE	2 FTE	2 FTE

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND	<u>\$0</u>	<u>(\$1,092,201) to</u> <u>(\$2,077,628)</u>	<u>(\$1,059,740) to</u> <u>(\$2,026,574)</u>	<u>(\$1,042,062) to</u> <u>(\$1,990,303)</u>
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<u>FISCAL IMPACT -</u> <u>Local Government</u>	FY 2021 (10 Mo.)	FY 2022	FY 2023	Fully Implemented (FY 2024)
	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>

FISCAL IMPACT - Small Business

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

FISCAL DESCRIPTION

For all tax years beginning on or after January 1, 2021, this act establishes a tax deduction in the amount of 100% of unreimbursed educator expenses incurred by an eligible educator, not to exceed \$500.

FISCAL DESCRIPTION (continued)

An eligible educator is defined as an individual who is a kindergarten through grade twelve teacher, instructor, counselor, principal, or aide in a school for at least 900 hours during a school year, or is a teacher in an early childhood education program.

Educator expenses are defined as expenses incurred as a result of the participation by the educator in professional development courses related to the curriculum in which the educator provides instruction, and expenses in connection with books, supplies, computer equipment and other equipment, and supplementary materials used by the eligible educator in the classroom. (Section 143.121)


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 & Planning Division
Missouri Department of Revenue
University of Missouri's Economic & Policy Analysis Research Center



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February 20, 2020



Ross Strope
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February 20, 2020