COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 3892S.03I
Bill No.: SB 993
Subject: Taxation and Revenue - Income; Saint Louis City
Type: Original
Date: March 25, 2024

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

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND			
FUND AFFECTED	FY 2025	FY 2026	FY 2027
General Revenue*	$0	$0 or Up to $888,043	$0 or Up to $888,043
Total Estimated Net Effect on General Revenue	**$0**	**$0 or Up to $888,043**	**$0 or Up to $888,043**

*Oversight notes the provisions of this proposal represent only 1 of 10 potential rate reductions. The potential savings to the state's General Revenue Fund would stem from a reduction in the amount of earnings taxes paid and subsequently used as a deduction in calculating a taxpayer's state income tax liability.

ESTIMATED NET EFFECT ON OTHER STATE FUNDS			
FUND AFFECTED	FY 2025	FY 2026	FY 2027
Total Estimated Net Effect on Other State Funds	**$0**	**$0**	**$0**

Numbers within parentheses: () indicate costs or losses.

ESTIMATED NET EFFECT ON FEDERAL FUNDS			
FUND AFFECTED	FY 2025	FY 2026	FY 2027
Total Estimated Net Effect on All Federal Funds	**$0**	**$0**	**$0**

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)			
FUND AFFECTED	FY 2025	FY 2026	FY 2027
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 2025	FY 2026	FY 2027
Local Government*	**$0 or (Up to $15,734,450)**	**$0 or (Could exceed $31,468,900)**	**$0 or (Could exceed $31,468,900)**

*Oversight notes the provisions of this proposal represent only 1 of 10 potential rate reductions.

FISCAL ANALYSIS

ASSUMPTION

§92.120 – Earnings Taxes

Officials from the **Office of Administration - Budget and Planning (B&P)** state for all tax years beginning 2025, the St. Louis City earnings and payroll taxes shall be reduced over several years. Each reduction shall be by 0.1% and more than one reduction may occur per year. Reductions will continue until both taxes have been fully phased-out.

To trigger a reduction, the "annual revenue received" by St. Louis City government must be 3% greater than the amount received in the prior fiscal year. B&P notes that the term "annual revenue received" includes all types of revenues, regardless of use limitations on such revenues.

B&P notes that this proposal indicates that more than one reduction may occur per year, but does not specify how multiple reductions would be triggered.

In any year that a reduction is triggered, 50% of the growth in "annual revenue received" must be deposited into the newly created "Earnings Tax Reserve Fund". B&P notes that this provision uses the phrase "annual revenues received" which includes revenues that are designated by law for specific purposes. Revenues in the fund are to be used to offset revenue declines caused by the tax rate reductions. If excess money is in the fund, the City may refund that money to taxpayers.

B&P is unable to estimate a precise impact from this proposal per year because it is unknown when or if, one or more reductions will occur. However, B&P is able to estimate the impact for each 0.1% reduction in the tax rates and the fully implemented impact.

Using data published by St. Louis City, B&P determined that the city collected $61,593,000 in business earnings tax, $162,872,000 in individual earnings tax, and $45,112,000 in payroll taxes. B&P notes that the earnings tax rate is currently 1.0%, while the payroll tax rate is 0.5%.

Therefore, B&P estimates that a 0.1% reduction may reduce revenues to the city by $16,287,200 for the individual earnings tax, $6,159,300 for the business earnings tax, and $9,022,400 for the payroll tax.

B&P notes that individuals and businesses are able to deduct the taxes paid to the city on their Missouri state income tax. Based on 2021 tax return data, B&P determined that 28.3% of individual itemize their return. For the purpose of this fiscal note, B&P assumes that 100% of businesses also deduct these taxes. In addition, B&P apportioned out the taxes paid by businesses between corporations (51.0%) and pass-through (49.0%) businesses, based on annual payroll data published by the U.S. Census Bureau, in order to determine the correct state income tax rate.

Therefore, B&P estimates that a 0.1% reduction to the earnings and payroll taxes may increase GR by $851,892 to $888,043 (depending on the individual income tax rate). Table 1 shows the estimated state and local impact.

Table 1: Estimated Impact per 0.1% Rate Reduction

Tax	GR Impact Low	GR Impact High	St. Louis City
Individual Earnings Tax	$207,417	$221,245	($16,287,200)
Business Earnings Tax	$261,467	$270,524	($6,159,300)
Payroll Tax	$383,007	$396,274	($9,022,400)
Total	**$851,892**	**$888,043**	**($31,468,900)**

Once fully implemented, B&P estimates that this proposal could increase GR by $6,603,879 annually through fewer deductions. This proposal may also decrease St. Louis City revenues by $269,577,000 annually. Table 2 shows the estimated fully implemented impact.

Table 2: Estimated Fully Implemented Impact

Tax	GR Impact	St. Louis City
Individual Earnings Tax	$2,074,175	($162,872,000)
Business Earnings Tax	$2,614,667	($61,593,000)
Payroll Tax	$1,915,037	($45,112,000)
Total	**$6,603,879**	**($269,577,000)**

Officials from the **Department of Revenue (DOR)** state the following:

Currently the City of Kansas City and St. Louis City have adopted an earnings tax on the residents of their district. This proposal would require that St. Louis City reduce its earnings tax by one-tenth of a percent based on certain revenue triggers. Currently the St. Louis City earnings tax is 1%.

This proposal also requires that should the revenue cause a reduction in the earnings tax rate, 50% of the increased revenue received has to be deposited into an Earnings Tax Reserve Fund. This proposal delineates the uses of the money in the Fund.

The DOR does not collect or distribute earnings tax for any City.

This proposal starting January 1, 2025, would require the St. Louis City earnings and payroll taxes to be reduced over several years based on delineated revenue triggers set in this proposal. The reductions are to be in increments of 0.1% and more than one may occur each year. The reductions are to continue until the St. Louis City earnings tax is eliminated.

If annual revenue received by St. Louis City is greater than 3% higher than the previous year, the trigger is activated, and their earnings tax will be reduced. This proposal, however, allows all income received by the city to be included and not just income from the earnings tax. When the revenue is received that causes the trigger, 50% of the excess funding is to be deposited into a newly created Earnings Tax Reserve Fund. Revenue in the fund is to be used to offset the reduction in the earnings tax with any remaining refunded back to the taxpayers who pay earnings tax.

St. Louis City publishes data on the amount of business earnings and individual earnings tax they collect. They note they collected from the business earnings tax $61,593,000 in FY 2022 and they collected individual earnings tax of $162,872,000 and payroll tax of $45,112,000. Their current earnings tax rate is 1.0% while their payroll tax is 0.5%. DOR notes that they can not predict when exactly these reductions will occur. However, DOR notes that if these are reduced by 0.1% it would reduce the business earnings tax by $6,159,300, individual earnings tax by $16,287,200 and payroll taxes by $9,022,400.

Taxes paid to state and local government can be itemized on a taxpayer's individual income tax return. Using DOR's internal individual income tax system, DOR was able to determine that approximately 28.3% of all people itemize. For fiscal note purposes, DOR will be assuming that 100% of the eligible companies would be exempt. Using DOR's tax data, DOR knows that DOR can apportion the business funding to 51% to corporations and 49% to pass-through businesses.

When the citizens and businesses no longer owe this tax to the cities, they will no longer be able to subtract it off their MO individual income tax return. Therefore, if you reduce the local tax by 0.1% it will increase general revenue by $851,892 to $888,043.

Table 1: Estimated Impact per 0.1% Rate Reduction

Tax	GR Impact Low	GR Impact High	St. Louis City
Individual Earnings Tax	$207,417	$221,245	($16,287,200)
Business Earnings Tax	$261,467	$270,524	($6,159,300)
Payroll Tax	$383,007	$396,274	($9,022,400)
Total	**$851,892**	**$888,043**	**($31,468,900)**

Once fully implemented this is expected to have the following impact.

Table 2: Estimated Fully Implemented Impact

Tax	GR Impact	St. Louis City
Individual Earnings Tax	$2,074,175	($162,872,000)
Business Earnings Tax	$2,614,667	($61,593,000)
Payroll Tax	$1,915,037	($45,112,000)
Total	**$6,603,879**	**($269,577,000)**

Oversight does not have information to the contrary and therefore, Oversight will reflect the estimates as provided by the B&P and DOR.

Oversight notes the proposal begins with the tax years beginning January 1, 2025 which would be filed in FY 2026 at the earliest. Therefore, Oversight will reflect a possible reduction from B&P and DOR's numbers starting in FY 2026. Oversight is also unaware in what fiscal year this proposal could be fully implemented. Therefore, Oversight will only show impact in FYs 2026 & 2027.

Oversight also notes in subsections 2(3) and 3 an amount equal to fifty percent of the growth in annual revenue received for the year a reduction in taxes is made will be deposited into the Earnings Tax Reserve Fund by St. Louis City. Funds deposited into this fund shall be used to offset any reduction in revenues due to reductions in the rate of tax made. Oversight is unsure of when this provision would take place or how much would be deposited in the fund.

Also, if the balance in the fund exceeds the amount to offset reductions in revenue due to reductions in the rate of tax, St. Louis City may authorize refunds to taxpayers from such excess balance. Oversight will, therefore, reflect a $0 or negative unknown to this fund for St. Louis City.

Officials from **St. Louis City** state the Earnings Tax is the single largest source of City revenue amounting to over a third of the General Fund budget and as such is the largest single source of funding for City services, including the Police Department, Fire and EMS, Parks and Recreation, Streets and other departments. Net receipts in FY23 totaled just under $219M. The proposed legislation proposes a graduated reduction in the Earnings Tax rate based on an arbitrary and fixed rate of growth of City annual revenue. Furthermore, annual revenue is defined as "all revenue received from any source including but not limited to "taxes, fees, charges for services, grants, loans or other intergovernmental transfers, court fines and forfeitures, leases and investment income." In City finances, not all revenues are equal and many come with restrictions as to use. Proceeds from financings are restricted to the projects being financed, grants are likewise restricted as to purpose and are in many cases non-recurring. Enterprise fund revenues are likewise to be used for purposes related to those business like enterprises as opposed to funding general City services. In addition to restrictions as to use, the volatility and non-recurring nature of some of these revenues would negate the very premise of the underlying rate of growth for funding City services that the legislation contemplates.

Ultimately if enacted this legislation would lead to a reduction in Earnings Tax revenue without identifying a like and recurring source of revenue to replace it. The Earnings Tax is not only the largest single recurring source of City revenue but also has a historic growth rate exceeding that of both sales and property taxes. The proposed legislation would result in a loss of this substantial revenue source delivering a major blow to the City's credit and fiscal condition and seriously impairing the City's ability to continue to provide basic City services.

Officials from the **Department of Labor and Industrial Relations**, **Office of the State Courts Administrator** and the **Missouri Highway Patrol** 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.

FISCAL IMPACT – State Government	FY 2025 (6 Mo.)	FY 2026	FY 2027
GENERAL REVENUE			
Savings – from potential taxpayers who itemized their taxes and receive a .1% reduction in taxes §92.120	$0	$0 or Up to $888,043	$0 or Up to $888,043
ESTIMATED NET EFFECT ON GENERAL REVENUE	**$0**	**$0 or Up to $888,043**	**$0 or Up to $888,043**

FISCAL IMPACT – Local Government	FY 2025 (6 Mo.)	FY 2026	FY 2027
ST. LOUIS CITY			
Loss – of revenue from earnings tax reduction of .1% §92.120.2	$0 or (Up to $15,734,450)	$0 or (Up to $31,468,900)	$0 or (Up to $31,468,900)
Cost – potential refund to taxpayers for excess funds triggered by a 3% growth of annual revenue §92.120.3	$0	$0 or (Unknown)	$0 or (Unknown)
ESTIMATED NET EFFECT ON ST. LOUIS CITY FUNDS	**$0 or (Up to $15,734,450)**	**$0 or (Could exceed $31,468,900)**	**$0 or (Could exceed $31,468,900)**

FISCAL IMPACT – Small Business

This proposal could reduce and possibly eliminate the business earnings and payroll taxes in St. Louis City from this proposal.

FISCAL DESCRIPTION

Current law authorizes the cities of St. Louis and Kansas City to levy an earnings tax on the income of residents and nonresidents performing work in the city, with a rate not to exceed 1%. For all tax years beginning on or after January 1, 2025, this act provides that the rate of tax imposed in St. Louis City may be reduced over a period of years. Each reduction shall be by 0.1% and shall only occur if the amount of annual revenue received, as defined in the act, in the previous fiscal year is greater than the amount of annual revenue received in the fiscal year immediately previous to such fiscal year by at least 3%.

In any such year, an amount equal to 50% of the growth in annual revenue received for such year shall be deposited into the "Earnings Tax Reserve Fund", which is required to be created by the act. Revenues deposited into such fund shall be used to offset the reduction in revenues due to reductions in the rate of tax made pursuant to the act. If the balance in the fund exceeds the amount necessary to offset reductions in revenue due to reductions in the rate of tax, the governing body of the City may authorize refunds to taxpayers from such excess balance.

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
Department of Labor and Industrial Relations

NM:LR:OD

Department of Revenue
Missouri Highway Patrol
Office of the State Courts Administrator
St. Louis City

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