COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 3931-01
Bill No.: SB 1020
Subject: Taxation and Revenue-General and Income
Type: Original
Date: February 28, 2002

FISCAL SUMMARY

ESTIMATED NET EFFECT ON STATE FUNDS			
FUND AFFECTED	FY 2003	FY 2004	FY 2005
General Revenue	($16,420,579)	($62,586,900)	($98,047,823)
Total Estimated Net Effect on All State Funds	**($16,420,579)**	**($62,598,400)**	**($98,047,823)**

ESTIMATED NET EFFECT ON FEDERAL FUNDS			
FUND AFFECTED	FY 2003	FY 2004	FY 2005
None			
Total Estimated Net Effect on All Federal Funds	**$0**	**$0**	**$0**

ESTIMATED NET EFFECT ON LOCAL FUNDS			
FUND AFFECTED	FY 2003	FY 2004	FY 2005
Local Government	**$0**	**$0**	**$0**

Numbers within parentheses: ( ) indicate costs or losses.
This fiscal note contains 5 pages.

FISCAL ANALYSIS

ASSUMPTION

Officials of the **Department of Revenue (DOR)** state this legislation phases in an earned income tax credit on the Missouri income tax return. For tax year beginning on January 1, 2003, a resident individual is authorized a state earned income tax credit equal to ten percent of the Federal earned income tax credit. Beginning January 1, 2004, a taxpayer is authorized a state earned income tax credit equal to fifteen percent, and beginning January 1, 2005, a taxpayer is authorized a state earned income tax credit equal to twenty percent of the Federal earned income tax credit. If the credit exceeds the taxpayer's liability, the credit may be refunded or carried forward. The DOR is required to notify any taxpayer who potentially may be eligible for the tax credit and who did not claim the credit on the state tax return.

According to the Federal Statistics of Income Bulletin, there are 379,333 federal returns filed by Missouri residents claiming an earned income tax credit. DOR assumes this credit will have an extra 20 second impact on all returns processed. The Division of Taxation will need one temporary tax season employee ($8 an hour) for every 75,000 returns filed with this credit and one tax season employee for every 2,000 pieces of correspondence received regarding the credit. The DOR will also need one Tax Processing Tech I for every 20,000 additional errors generated by this credit.

The Customer Assistance Bureau will need additional tax assistance field personnel to handle the walk in questions until the credit is maximized. One Field Agent is requested for every additional 1,285 walk-ins per year. Also, the Customer Assistance Bureau anticipates the call volume to increase. A telephone collector can handle 2,000 calls per month, therefore, one Telephone Collector is requested for every 24,000 additional calls received regarding this credit.

The DOR will request at this time 5 Temporary Tax Season employees to key and process the tax credits in order to maintain current processing times. All other FTE needed will be requested through the normal budget process once the DOR has processed the credit and has numbers to determine the amount of errors and correspondence received, and the increase in telephone calls and walk-ins.

DOR assumes this legislation will require modifications to the individual income tax systems. The Division of Taxation estimates these modifications, including programming changes, will require 1,125 hours of overtime at a cost of $29,422. Modifications to the income tax returns and schedules will be completed with existing resources. State Data Center charges will increase due to the additional storage and fields to be captured. Funding in the amount of $3,657 is requested for implementation costs.

ASSUMPTION (continued)

Officials of the **Office of Administration, Budget and Planning (BAP)** assume this proposal creates a state income tax credit equal to 10% in CY03, 15% in CY04, and 20% thereafter of the Federal earned income tax credit.

BAP assumes that taxpayers will not adjust their withholdings in FY03 to take advantage of this credit. The estimate is based on the amount of earned income tax credit claimed in Missouri in 1999 from the Spring 2001 Statistics of Income. Annual growth of 4% is assumed, based on U.S. Treasury forecasts. The lower limit is based on the assumption that only 85% of taxpayers that use the federal credit will use the state credit. The upper limit assumes 100% of taxpayers that use the federal credit will use the state credit. When the credit is fully phased in it will cost $130.9 to $154.0 million annually.

According to officials at the **University of Missouri, Research Center (UMRC)**, there was a total of $609 million in Federal earned income tax credits filed with a Missouri address for 2000. Assuming a 4.5% growth rate would generate Federal earned income tax credits of $694.8 million in FY03 and $726 million in FY04. Using the proposed percentages for a Missouri earned income tax credit for tax year 2003 filed in FY04, and tax year 2004 filed in FY05; would calculate to $69.5 million state revenue loss in FY04 and would yield a $108.9 million revenue loss in FY05. The revenue loss would be $151.7 million for FY06. For these estimates, UMRC assumes the Federal government would enact no further changes in the earned income tax credit.

For purposes of this fiscal note, **Oversight** assumes for FY04 and FY05, 90% of taxpayers who use the Federal credit will use the state credit. For FY06, Oversight assumes that 95% of taxpayers who use the federal credit will use the state credit. Oversight's estimate is based on the amount of earned income tax credit claimed in Missouri for tax year 2000 according to the University of Missouri, Research Center ($609,000,000). Oversight assumed an annual growth rate of 4.5%. Oversight's assumption is based on conversations with other states that currently have an earned income tax credit in place and the provision in this proposal that requires the Department of Revenue to notify potentially eligible filers.

Oversight assumes the DOR would require verification of eligibility. In the absence of such verification, total credits could be significantly greater than estimated. Oversight notes the long range cost of this proposal is expected to be greater than $150 million annually.

Oversight estimates a loss to the General Revenue Fund of $16.4 million for FY 2003 due to the possibility of reduced withholding and estimated income tax payments for calendar year 2003. Oversight assumes 25% of Missouri taxpayers would adjust payments, however it should be noted that this amount could be less depending on the taxpayers' awareness of this credit in determining state income tax and their desire to adjust withholdings or estimated payments.

ASSUMPTION (continued)

This proposal would result in a decrease in Total State Revenues.

FISCAL IMPACT - State Government	FY 2003 (10 Mo.)	FY 2004	FY 2005
GENERAL REVENUE FUND			
Loss to General Revenue Fund			
Earned Income Tax Credit	($16,387,500)	($62,550,000)	($98,010,000)
Cost - Department of Revenue			
Personal Service (5 Temps.)	$0	($36,900)	($37,823)
Expense and Equipment	$0	($11,500)	$0
Programming	($33,079)	$0	$0
Total Costs - DOR	($33,079)	($48,400)	($37,823)
ESTIMATED NET EFFECT ON GENERAL REVENUE FUND	**($16,420,579)**	**($62,598,400)**	**($98,047,823)**

FISCAL IMPACT - Local Government	FY 2003 (10 Mo.)	FY 2004	FY 2005
	$0	$0	$0

FISCAL IMPACT - Small Business

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

DESCRIPTION

This bill allows a state individual income tax credit equal to a percentage of any earned income tax credit claimed by the taxpayer on the Federal individual income tax return. The percentage of the Federal credit allowed will be 10% for tax year 2003, 15% for tax year 2004, and 20% for tax year 2005 and thereafter. Any amount of credit which exceeds the taxpayer's liability in any tax year will be refunded to the taxpayer or carried forward into future tax years.

KS:LR:OD (12/01)

DESCRIPTION (continued)

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
University of Missouri, Research Center
Office of Administration, Budget and Planning
Spring 2001 Statistics of Income

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