COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 1980-01
Bill No.: HB 1043
Subject: Taxation and Revenue - Income; Revenue Department
Type: Original
Date: March 31, 2015

Bill Summary: This proposal would require the Department of Revenue to adjust Missouri taxable income amounts used to determine income tax rates by the same amounts of percentage increases in the CPI for all years between 1931 and 2016.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND				
FUND AFFECTED	FY 2016	FY 2017	FY 2018	Fully Implemented*
General Revenue*	$0	$0	$0	($2,731,662,000)
Total Estimated Net Effect on General Revenue*	**$0**	**$0**	**$0**	**($2,731,662,000)**

* This proposal would be fully implemented in FY 2096.

ESTIMATED NET EFFECT ON OTHER STATE FUNDS				
FUND AFFECTED	FY 2016	FY 2017	FY 2018	Fully Implemented
Total Estimated Net Effect on Other State Funds	**$0**	**$0**	**$0**	**$0**

Numbers within parentheses: ( ) indicate costs or losses.
This fiscal note contains 9 pages.

ESTIMATED NET EFFECT ON FEDERAL FUNDS				
FUND AFFECTED	FY 2016	FY 2017	FY 2018	Fully Implemented
Total Estimated Net Effect on All Federal Funds	**$0**	**$0**	**$0**	**$0**

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)				
FUND AFFECTED	FY 2016	FY 201	FY 2018	Fully Implemented
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 2016	FY 2017	FY 2018	Fully Implemented
Local Government	**$0**	**$0**	**$0**	**$0**

FISCAL ANALYSIS

ASSUMPTION

Section 143.011, RSMo. - Personal Income Tax Rate Brackets:

Beginning with 2017, 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 2017, would be based on the inflation increase in 2016. 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 2016 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 (BAP)** assume this proposal would reduce Total State Revenues by $1,268.2 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.

BAP officials noted this proposal would require the individual income tax brackets to be adjusted for inflation from 1931 through 2016, 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 2015. For 2019 the tax rate brackets would be adjusted for inflation in 2018 and 2014.

This proposed additional adjustment would be applied for all years from 1931 - 2015 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)

BAP 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 2094. 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 2012 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.

BAP 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
2017	$0.0
2018	$3.1
2019	$12.2
2020	$20.4
2095	$1,268.2

ASSUMPTION (continued)

Officials from the **Department of Revenue (DOR)** assume this proposal would not have a fiscal impact on their organization but would reduce Total State Revenues.

DOR officials stated this proposal would adjust the income tax brackets based on the historical increase in the cost of living from 1931 to 2016 as measured by the Consumer Price Index for All Urban Consumers for the United States.

For tax years beginning January 1, 2017, the Department 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, 2016. For tax years beginning after January 1, 2018, the legislation would require the Department to make additional annual adjustments until each historical inflation increase from calendar years 1931 to 2016 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 2.9 percent to estimate the change to the tax brackets for this proposal. Using tax year 2012 data, the Department estimated that Total State Revenue could be reduced by as much as $1.25 billion per year when fully implemented.

Administrative Impact

DOR officials assume Personal Tax would require forms and programming changes, and withholding Tax would require revisions to the withholding tables and formula for the new tax rates.

IT impact

DOR officials noted because the effective date is in 2017, OA - ITSD (DOR) would require no additional programming. The system changes would be implemented in the new integrated revenue system.

ASSUMPTION (continued)

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 2017 would increase the size of the tax brackets by the same percentage as the inflation rate evident in the CPI from the calendar year 2016. 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 2016. Further, the proposal stated "When there was no inflation increase in the next immediate preceding year (counting backward from 2016), 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 noted that annual CPI data was recently released for calendar year 2014. In order to estimate the impact this bill would have on the 2017 and 2018 tax years' revenues we must forecast the inflation rate for 2015 and 2016. We estimate the inflation rate for 2015 at 2.6% and the inflation rate for 2016 at 3.3906%. Using these figures, EPARC prepared an adjusted rate bracket schedule

EPARC officials reported a baseline simulation using the most recent data on individual income tax for Missouri for 2013 and the current tax rate table, and stated that estimated Net Tax Due would be $5,124.717 million. A second simulation using the same data and the adjusted rate table provided an estimated Net Tax Due of $5,110.004 million, a reduction in Net Tax Due of $14.713 million from the baseline.

Oversight notes this revenue reduction would apply to 2017 individual income taxes which would be filed in FY 2018; however, this reduction is included in current law and will not be included in this fiscal note.

EPARC officials also provided an estimate of the fully implemented impact of this proposal based on their calculations that the fully implemented proposal would increase the tax rate brackets by the same percent as the percent increase in CPI evident from 1931 to 2016; to increments of $16,610 in the following manner. EPARC officials prepared a simulation using the same income tax as before with the adjusted tax rate brackets which indicated Net Tax Due would be $2,393.055 million, a reduction in Net Tax Due of $2,731.662 million from the baseline.

ASSUMPTION (continued)

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

Officials from the **Office of the Secretary of State (SOS)** assume 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 Secretary of State's Office 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, we also recognize that many such bills may be passed by the General Assembly in a given year and that collectively the costs may be greater than our office can sustain with our core budget. Therefore, we reserve 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.

Officials from the **Joint Committee on Administrative Rules** assume this proposal would not have a fiscal impact to their organization in excess of existing resources.

FISCAL IMPACT - State Government	FY 2016 (10 Mo.)	FY 2017	FY 2018	Fully Implemented *
GENERAL REVENUE				
Revenue reduction- Tax rate bracket adjustments	$0	$0	$0	($2,731,662,000)
ESTIMATED NET EFFECT TO GENERAL REVENUE*	**$0**	**$0**	**$0**	**($2,731,662,000)**

* This proposal would be fully implemented in FY 2096.

FISCAL IMPACT - Local Government	FY 2016 (10 Mo.)	FY 2017	FY 2018	Fully Implemented
	$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, 2017, this proposal would require 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 2016.

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

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