

COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 0553-01
Bill No.: HB 189
Subject: Education, Elementary and Secondary; Taxation and Revenue - General
Type: Original
Date: January 20, 2017

Bill Summary: This proposal creates an educational savings plan for K-12 educational expenses.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND			
FUND AFFECTED	FY 2018	FY 2019	FY 2020
General Revenue	Unknown or (\$4,066,221 to \$6,674,440)	Unknown or (\$7,717,031 to \$12,933,470)	Unknown or (\$15,218,772 to \$25,651,650)
Total Estimated Net Effect on General Revenue	Unknown or (\$4,066,221 to \$6,674,440)	Unknown or (\$7,717,031 to \$12,933,470)	Unknown or (\$15,218,772 to \$25,651,650)

ESTIMATED NET EFFECT ON OTHER STATE FUNDS			
FUND AFFECTED	FY 2018	FY 2019	FY 2020
Total Estimated Net Effect on <u>Other</u> State Funds	\$0	\$0	\$0

Numbers within parentheses: () indicate costs or losses.
This fiscal note contains 12 pages.

ESTIMATED NET EFFECT ON FEDERAL FUNDS			
FUND AFFECTED	FY 2018	FY 2019	FY 2020
Total Estimated Net Effect on <u>All</u> Federal Funds	\$0	\$0	\$0

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)			
FUND AFFECTED	FY 2018	FY 2019	FY 2020
General Revenue	5 FTE	5 FTE	5 FTE
Total Estimated Net Effect on FTE	5 FTE	5 FTE	5 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 2018	FY 2019	FY 2020
Local Government	\$0	\$0	\$0

FISCAL ANALYSIS

ASSUMPTION

§166.485 - §166.496 Missouri K-12 Education Savings Program

Officials at the **Office of Administration's Division of Budget and Planning (B&P)** assume this proposal creates an education savings program for participants who wish to send beneficiaries of the program to any private or public school or who wish to pursue a home school curriculum. Qualifying contributions to education savings accounts are exempt from taxation by the state or any of its political subdivisions. The minimum contribution level is \$25; no specific maximum contribution level per participant or household is set by the proposal.

The annual contributions and income made to the savings program are deductible from Missouri adjusted gross income. Moneys accruing to and deposited in individual savings accounts are not deemed part of Total State Revenue and expenditure of such revenues is not a state government expense under Article X, Section 20, of the Missouri Constitution. However, the extent to which contributions and their earnings are deducted from adjusted gross income will reduce General and Total State Revenue, and will impact the calculation under Article X, Section 18(e).

B&P notes the number of participants and amounts of any contributions is unknown, but are estimated below:

Public Schools:

According to data available from DESE, there were 887,358 enrolled public K12 students in 2014. Various media reports suggest the cost of school supplies is roughly \$100 per student. This suggests \$88,735,800 in potential costs. Based on data available regarding cafeteria plan participation, B&P estimates 20-50% of eligible taxpayers may choose to use the savings plan. At the current 6% income tax rate, this could reduce revenues – see table below.

Public Schools		
Number of Students in Public School	887,358	
Average cost of school supplies	\$100	
Total Avg cost of Public	\$88,735,800	
Likely % participating	20%	50%
Potential contributions	\$ 17,747,160	\$ 44,367,900
Estimated Loss to GR 6%	\$ 1,064,830	\$ 2,662,074

ASSUMPTION (continued)

Private Schools:

According to the Private School Review, there are 117,372 private school students in Missouri. B&P assumes their largest qualifying costs would be tuition, which the review estimates as \$6,487 for elementary students, and \$12,095 for high school students. Based on available Census data, B&P estimates there are 83,957 private elementary students, and 33,415 private high school students. B&P further assumes that roughly 20% of these tuition costs would be covered by scholarships or other assistance. Using the 20-50% range above, at the current 6% income tax rate, this could reduce revenues – see table below.

Private Schools		
Number of Students in Private School	117,372	
Estimated # Elementary	83,957	
Estimated # Secondary	33,415	
Avg Cost of Elementary in MO	\$ 6,487	
Avg Cost of Secondary in MO	\$ 12,095	
Percent of assistance	20%	
Total Avg Cost of Elementary (less assistance)	\$ 435,703,247.20	
Total Avg Cost of Secondary (less assistance)	\$ 323,323,540	
Total Cost	\$ 759,026,787	
Likely % participating	20%	50%
Potential Contributions	\$ 151,805,357	\$379,513,394
Estimated Loss to GR	\$ 9,108,321	\$ 22,770,804

Therefore, it is possible this program may reduce General and Total State Revenues between \$10.2 million and \$25.4 million annually. The actual rates of participation, and any caps set by the Board, could impact these estimates.

B&P notes the existing MOST program for higher education savings is a comparable program. Using MOST data on tax filings in 2014 supplied by DOR, approximately \$15 million was claimed as contributions to MOST accounts by taxpayers. At the current 6% rate, the loss to

ASSUMPTION (continued)

General and Total State Revenues is smaller than the estimate above, but that program has statutory caps on annual contributions, and the universe of families saving for higher education is likely smaller.

Officials at the **Department of Revenue (DOR)** assume §166.485 through §166.496 establish the "Missouri K-12 Education Savings Program." This program is essentially the same as the Missouri Higher Education Savings Program (MOST), except that there is no federal tax advantage to the K-12 program. Participants in the savings program, i.e. those contributing to education beneficiaries, can transfer a portion (at least \$25) of their Missouri income tax returns to a beneficiary account. DOR is required to draft the forms for doing so. DOR will require form changes and programming. The Integrated Tax System will require additional funding in the amount of \$65,426 to implement the provisions of this legislation.

The Personal Tax Division will require two Revenue Processing Technicians I (\$27,185) for correspondence and error correction. The Collections & Tax Assistance Division will see additional customer contacts about the direct deposit option and notice of adjustments. The section requires one Tax Collection Technicians I (\$27,185) for every 15,000 contacts annually on the non-delinquent tax line. This technician requires CARES equipment and license.

Assets in the savings program are exempt from state tax if they are used for qualified educational expenses, and annual contributions to a beneficiary account are deductible from Missouri adjusted gross income beginning January 1, 2018; if contributions to the savings program are not used for qualified educational expenses, they are to be added back to Missouri adjusted gross income (presumably by the participant who previously deducted them). §166.491 will require IT and other actions by DOR.

Beginning with tax year 2018, the legislation exempts the assets of the savings program from tax by the state or political subdivisions. The provisions of this section also specify that income earned from the savings programs not be subject to income tax. The board subtracts contributions in order to determine Missouri adjusted gross income.

The Collections & Tax Assistance Division will see additional customer contacts about the direct deposit option and notice of adjustments. The section requires two Tax Collection Technicians I (\$27,185); one for every 15,000 contacts annually on the non-delinquent tax line and one for every 15,000 on the delinquent tax line. Each technician requires CARES equipment and license.

A similar program that allows for a subtraction from adjusted gross income for amounts donated to a MOST/529 Account for higher education was claimed on approximately 50,000 returns in

ASSUMPTION (continued)

the amount of \$250 million for tax year 2014. This legislation differs as it has no cap on the deduction, but the Department assumes that the differences in the amounts saved by individuals could be similar. If taxpayers deduct a similar amount on their Missouri Individual Income Tax returns the Department assumes a negative impact of \$15 million per year (\$250 million x 6%). The Department of Elementary and Secondary Education or the Office of Administration, Budget and Planning, may have more accurate numbers on actual amounts spent on K-12 education.

Participants may contribute personal income tax refunds to an account established in this legislation. The contribution must be at least \$25 and only for the tax year of the refund. The Department prescribes the specific form and the taxpayer must file the form with their tax return.

Oversight has, for fiscal note purposes only, changed the starting salary for the Revenue Processing Technicians I (from \$27,185 to \$24,360) and for the Taxation and Collection Technicians I (from \$27,185 to \$24,360) to correspond to the second step above minimum for comparable positions in the state's merit system pay grid. This decision reflects a study of actual starting salaries for new state employees and policy of the Oversight Subcommittee of the Joint Committee on Legislative Research.

Oversight notes the educational savings program can accept grants, gifts, legislative appropriations and other money. Oversight is unable to determine how much will be received and for fiscal note purposes is showing the impact as Unknown.

Oversight notes this program imposes a penalty equal to or greater than 10% of the earnings on the account if a distribution is not used properly. Oversight is unable to estimate the amount of penalty money that will be collected and for fiscal note purposes is showing the impact as Unknown.

Oversight notes this educational savings program is similar to the MOST 529 program currently run by the state. Oversight requested information on the number of participants (in 2016) in the MOST 529 program. Below is the information:

ASSUMPTION (continued)

Contribution Group	Total Accounts in Group	Overall Share
No 2016 contributions	66,837	42.50%
\$1-\$100	6,240	4.00%
\$100-\$499	16,960	10.80%
\$500-\$999	16,839	10.70%
\$1,000 - \$1,999	17,822	11.30%
\$2,000 - \$4,999	16,421	10.50%
\$5,000 - \$7,999	6,257	4.00%
\$8,000 - \$13,999	6,530	4.20%
\$14,000 - \$15,999	755	.50%
\$16,000 - \$27,999	1,953	1.20%
\$28,000 and over	515	.30%
Total	157,129	100%

Oversight notes this proposal allows the contributions to the educational savings program to be used for qualifying educational expenses. Those expenses include tuition and fees at public and private schools, books, supplies, computers, tutoring and home school curriculums.

Due to the time frame for the creation of the rules regarding this program, **Oversight** for fiscal note purposes, is showing the expense of the program as 25 % in FY 2018, and 50% in FY 2019 of the estimate provided by B&P (\$15,000,000 to \$25,432,878). However, for example should the same 32% that currently give over \$1,000 in the MOST 529 program choose to save \$1,000 in the educational savings program, the educational savings program could cost as much as \$50,281,000 (50,281 [32% of account holders in MOST] x \$1,000).

Officials at the **Office of the State Treasurer** assume that because of the unforeseen ability to predict the need for starting appropriations to get the savings program off the ground, the STO estimates an impact from General Revenue of \$0 to an unknown amount.

ASSUMPTION (continued)

Officials at the **Department of Elementary and Secondary Education** assume depending upon the actions of the board, this could result in costs to the department; however, we would not expect costs to be significant.

§166.486 Missouri K-12 Education Savings Board

Officials at the **Department of Economic Development, Missouri House of Representatives, Missouri Senate, Office of the Governor, Office of Administration's Division of Accounting and Commissioner's Office** and the **Joint Committee on Administrative Rules** each assume there is no fiscal impact from this proposal to their respective organization.

Officials from the **Office of the Secretary of State (SOS)** state 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 SOS 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, the SOS also recognizes that many such bills may be passed by the General Assembly in a given year and that collectively the costs may be in excess of what the office can sustain with the core budget. Therefore, the SOS reserves 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.

Oversight assumes the SOS could absorb the costs of printing and distributing regulations related to this proposal. If multiple bills pass which require the printing and distribution of regulations at substantial costs, the SOS could request funding through the appropriation process.

<u>FISCAL IMPACT - State Government</u>	FY 2018 (10 Mo.)	FY 2019	FY 2020
GENERAL REVENUE			
<u>Revenue</u> - Grants and gifts §166.486.1(6)	Unknown	Unknown	Unknown
<u>Revenue</u> - penalty fees §166.490	Unknown	Unknown	Unknown
<u>Revenue Reduction</u> - contributions and earned income in savings programs are tax free §166.491.1	(\$3,750,000 to \$6,358,219)	(\$7,500,000 to \$12,716,439)	(\$15,000,000 to \$25,432,878)
<u>Cost</u> - Administration & Operation of program including start up costs §166.4863.1(11)	(Unknown over \$100,000)	(Unknown)	(Unknown)
<u>Cost</u> - DOR			
Personal Service	(\$101,500)	(\$123,018)	(\$124,248)
Fringe Benefits	(\$73,177)	(\$88,175)	(\$88,541)
Equipment and Expenses	<u>(\$41,544)</u>	<u>(\$5,838)</u>	<u>(\$5,983)</u>
<u>Total Cost</u> - DOR	<u>(\$216,221)</u>	<u>(\$217,031)</u>	<u>(\$218,772)</u>
FTE Change - DOR	5 FTE	5 FTE	5 FTE
ESTIMATED NET EFFECT ON GENERAL REVENUE	Unknown or (\$4,066,221 to <u>\$6,674,440</u>)	Unknown or (\$7,717,031 to <u>\$12,933,470</u>)	Unknown or (\$15,218,772 to <u>\$25,651,650</u>)
Estimated Net FTE Change on General Revenue	5 FTE	5 FTE	5 FTE

FISCAL IMPACT - Local Government

FY 2018
(10 Mo.)

FY 2019

FY 2020

\$0

\$0

\$0

FISCAL IMPACT - Small Business

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

FISCAL DESCRIPTION

This bill creates the "Missouri K-12 Education Savings Program" and establishes the "Missouri K-12 Education Saving Board."

Missouri K-12 Education Savings Board (§166.486) - The Missouri K-12 Education Savings Board members are specified in the bill and include the State Treasurer, Commissioner of Education, Commissioner of the Office of Administration, Director of the Department of Economic Development, and one member appointed by the Speaker of House of Representatives.

The board must develop and implement the savings program, any educational programs, and materials for participants of the savings program. The duties and responsibilities of the board are specified in the bill and include entering into financial agreements with financial institutions, investing the funds, and making all deposits and distributions. The board shall meet at least once per quarter, have four members present for a quorum, and a member may appoint a proxy for a specified meeting.

Savings Program Agreements (§166.487) - This bill allows the board to enter into savings program agreements with participants on behalf of beneficiaries. The agreements must contain specified information including the terms and conditions, method of calculating the return on the contribution, disclosure of the risk of the investment, and be presented to participants in language easily understandable by the public. The board shall establish contribution limits and a minimum length of time that contributions and earnings must be held by the savings program, as specified in the bill.

Contributions, Earnings, and Cancellation (§166.488, §166.489, §166.490, and §144.491) - A participant may elect to contribute all or part of his or her income tax refund into the savings program. The amount deposited must be a minimum of \$25 and the Department of Revenue shall determine the amount of accounts that the taxpayer may contribute.

If the taxpayer's refund is offset to pay amounts owed by him or her the contribution will not be

FISCAL DESCRIPTION (continued)

made to an account.

Contributions from a participant will be deposited and promptly invested by the board. The contributions and subsequent earnings may be used for qualified K-12 educational expenses, as described in the bill, and will not be considered income for purposes of financial aid eligibility under any state student aid program, is tax exempt, and will be subtracted when determining Missouri adjusted gross income.

A participant may cancel his or her agreement at will. The board must impose at least a 10% penalty for any distribution that is not used exclusively for qualified educational expenses or used as otherwise specified in the bill.

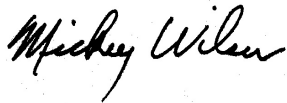
The assets of the savings program may only be used as specified in these provisions and in accordance with the participation agreement.

Review of the Program (§166.494, §166.495 and §166.496) - The Director of Investment of the State Treasurer's Office will review the financial status, investment policy of the savings program, participation rate, and viability of the program on a semiannual basis. The director shall submit a report to the board annually. Any funds deposited into individual savings accounts and the subsequent accruals will not be part of total state revenues and all personally identifiable information of participants and beneficiaries will be confidential.

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 Economic Development
Department of Elementary and Secondary Education
Department of Revenue
Joint Committee on Administrative Rules
Missouri House of Representatives
Missouri Senate
Office of Administration
 Division of Budget and Planning
 Division of Accounting
 Commissioner's Office
Office of the Governor
Office of the Secretary of State
Office of the State Treasurer



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