

COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 1176-01
Bill No.: HB 582
Subject: Taxation and Revenue - General; Taxation and Revenue - Income; Military Affairs
Type: Original
Date: February 16, 2017

Bill Summary: This proposal would allow an individual to deduct income earned through active military duty, the National Guard, or reserve components of the Armed Forces of the United States from their Missouri adjusted gross income.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND			
FUND AFFECTED	FY 2018	FY 2019	FY 2020
General Revenue	(\$58,665,426)	(\$29,300,000)	(\$29,300,000)
Total Estimated Net Effect on General Revenue	(\$58,665,426)	(\$29,300,000)	(\$29,300,000)

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

Numbers within parentheses: () indicate costs or losses.

This fiscal note contains 7 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
Total Estimated Net Effect on FTE	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 2018	FY 2019	FY 2020
Local Government	\$0	\$0	\$0

FISCAL ANALYSIS

ASSUMPTION

Officials from the **Office of Administration - Division of Budget and Planning (BAP)** assume this proposal would exempt military pay for National Guard and reserve components of the armed forces from state income tax. The exemption would be effective January 1, 2016.

BAP officials included data provided by the Missouri National Guard. Estimated total pay for Missouri National Guard soldiers was \$416.0 million in 2013, \$420.2 million in 2014, and \$371.9 million in 2015, for an average total pay of \$402.7 million.

BAP officials also stated that based on other information from the Missouri National Guard, the total average traditional pay for National Guard soldiers is \$126.9 million. BAP officials assumed that National Guard and other armed forces reserve members are paid similar salaries of approximately \$11,000 per year. In 2015, there were 7,820 armed forces reserve soldiers stationed in Missouri. Therefore, BAP officials estimated that armed forces reserve soldiers earned a total of \$85.1 million in Missouri during 2015.

Based on the above information, BAP officials estimated total military income of $(\$402.7 \text{ million} + \$85.1 \text{ million}) = \487.8 million would become exempt from Missouri income tax if this proposal is implemented. Since income tax exemptions do not reduce Total State Revenues (TSR) on a dollar for dollar basis, BAP officials estimated this proposal would reduce TSR by $(\$487.8 \text{ million} \times 6\%) = \29.3 million per year.

This proposal would allow the exemption to begin January 1, 2016. BAP officials noted this proposal would not be in effect until August 28, 2017. Since the effective date would be slightly more than halfway through 2017 (FY 2018), BAP officials assume that individuals would request refunds for 2016 and 2017 overpayments beginning August 28, 2017 (FY 2018). Therefore, BAP officials assumed that TSR and General Revenue for FY 2018 would be reduced by the full amount of the exemption from tax year 2016 and 2017, as well as half the impact from tax year 2018.

Oversight is aware that some filers would reduce their payroll withholding or estimated tax payments in anticipation of an income tax reduction but will assume for fiscal note purposes the revenue reductions should be reflected in the fiscal year in which the returns are filed. Refund claims for 2016 tax returns filed in FY 2017 would be submitted in FY 2018, as well as tax returns for 2017. The revenue reduction for FY 2018 would be $(\$29.3 \text{ million} \times 2) = \58.6 million . Tax returns for 2018 would be filed in January 2019 (FY 2019).

ASSUMPTION (continued)

Officials from the **Department of Revenue (DOR)** assume this proposal would allow for a deduction from Missouri adjusted gross income for salary or compensation in any form earned as a member of the National Guard or reserve components of the armed forces. DOR officials estimated a negative impact on Total State Revenue of \$29.2 million per year when fully implemented.

DOR officials determined there are approximately 19,500 Missouri residents that are part of the military reserve forces, 11,700 whom serve in the National Guard and 7,800 whom serve in the reserves. According to the Missouri National Guard Annual Reports for the last three years the average total pay of Missouri guardsman was \$402.7 million, DOR officials estimate average military reserve pay of \$126.9 million under the assumption that reservists are compensated in a similar fashion as the National Guard's traditional pay only.

DOR officials provided the following table of National Guard pay.

Year	National Guard Total Pay	National Guard Traditional Pay	Reserve Pay
2013	\$416,000,000	\$133,800,000	\$0
2014	\$420,200,000	\$127,600,000	\$0
2015	\$371,900,000	\$119,400,000	\$0
Average	\$402,700,000	\$126,900,000	\$84,600,000
Members	11,700	11,700	7,800
Average Pay	\$34,419	\$10,846	\$10,846

ASSUMPTION (continued)

Administrative Impact:

DOR officials assume Personal Tax would require two additional Revenue Processing Technicians I (Range 10, Step L) for every 19,000 error corrections and for every 2,400 pieces of correspondence. In addition, Collections and Tax Assistance would require two additional Tax Collection Technicians I (Range 10, Step L); one for every additional 15,000 contacts on the delinquent tax line and one for every 15,000 additional contacts on the non-delinquent tax line. Each technician would require CARES equipment and license.

In total, the DOR estimate of administrative cost to implement this proposal including four additional employees and the related benefits, equipment, and expense totaled \$185,056 for FY 2018, \$188,434 for FY 2019, and \$189,878 for FY 2020.

Oversight notes this proposal would change a limited number of computations on income tax returns and would not be expected to have a significant impact on the number of returns filed, except for refund claims that would presumably be filed for 2016 taxes paid in FY 2017.

Oversight assumes there would not be a significant number of additional errors resulting from the changes in this proposal, and assumes existing DOR staffing would be adequate to implement this proposal. If unanticipated additional costs are incurred or if multiple proposals are implemented that increase DOR costs or the workload for DOR employees, resources could be requested through the budget process.

DOR officials assume that implementing this proposal would result in an additional funding requirement of \$65,426 for the Integrated Tax System.

Oversight will include the DOR estimate of additional IT cost for the Integrated Tax System in this fiscal note.

Officials from the **University of Missouri - Economic and Policy Analysis Research Center** stated they were unable to obtain the specific military pay information needed to prepare an estimate of the fiscal impact of this proposal.

Officials from the **Office of the Secretary of State**, the **Joint Committee on Administrative Rules**, and the **Department of Public Safety - Missouri Veterans Commission** assume this proposal would have no fiscal impact on their organizations.

<u>FISCAL IMPACT - State Government</u>	FY 2018 (10 Mo.)	FY 2019	FY 2020
GENERAL REVENUE FUND			
<u>Costs - DOR</u>			
Programming changes	(\$65,426)	\$0	\$0
<u>Revenue Reduction</u>			
Income tax exemption for military income earned by members of the National Guard and armed forces reserve components.	<u>(\$58,600,000)</u>	<u>(\$29,300,000)</u>	<u>(\$29,300,000)</u>
ESTIMATED NET EFFECT ON GENERAL REVENUE FUND	<u>(\$58,665,426)</u>	<u>(\$29,300,000)</u>	<u>(\$29,300,000)</u>

<u>FISCAL IMPACT - Local Government</u>	FY 2018 (10 Mo.)	FY 2019	FY 2020
	<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

The proposed legislation would allow an individual to deduct income earned through active military duty, the National Guard, or reserve components of the Armed Forces of the United States from Missouri adjusted gross income.

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 Public Safety
 Missouri National Guard
Department of Revenue
University of Missouri
 Economic and Policy Analysis Research Center



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