COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 0448-08
Bill No.: SCS for SB 18
Subject: Taxation and Revenue; Higher Education
Type: Original
Date: February 3, 2003

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND			
FUND AFFECTED	FY 2004	FY 2005	FY 2006
General Revenue	($59,283 to Unknown)	($56,399 to Unknown)	($57,814 to Unknown)
Total Estimated Net Effect on General Revenue Fund*	**($59,283 to UNKNOWN)**	**($56,399 to UNKNOWN)**	**($57,814 to UNKNOWN)**

***Expected to exceed $100,000 annually**

ESTIMATED NET EFFECT ON OTHER STATE FUNDS			
FUND AFFECTED	FY 2004	FY 2005	FY 2006
Total Estimated Net Effect on Other State Funds	**$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 2004	FY 2005	FY 2006
Total Estimated Net Effect on All Federal Funds	**$0**	**$0**	**$0**

ESTIMATED NET EFFECT ON LOCAL FUNDS			
FUND AFFECTED	FY 2004	FY 2005	FY 2006
Local Government	**$0**	**$0**	**$0**

FISCAL ANALYSIS

ASSUMPTION

Officials from the **Office of the Governor** assume this proposal would not fiscally impact their agency.

Officials of the **Department of Revenue (DOR)** did not respond to our fiscal note request for this substitute. However in a prior response to SB 18, DOR stated that currently, the subtraction for the MOST program is limited to $8,000 per person. This legislation expands the limit to $8,000 per person or $16,000 if married filing joint. Therefore, married taxpayers filing a combined return will be able to deduct up to $16,000 worth of contributions, although only one spouse earns income. Also, this legislation expands the subtraction to allow any program qualified under section 529 of the IRC. DOR assumes this will include out of state programs.

DOR assumes Personal Tax will need to verify the documentation on each subtraction and handle additional correspondence. Personal Tax will need one Tax Processing Tech for every 30,000 additional deductions claimed and one Tax Processing Tech for every 3,000 additional pieces of correspondence received on this legislation. DOR defers to the estimated revenue impact prepared by the State Treasurers Office.

ASSUMPTION (continued)

Officials of the **Office of Administration, Budget and Planning (BAP)** assume the legislation will decrease total state revenue due to the expansion of the type of IRC Section 529 assets exempt from state taxes. BAP defers to the STO estimate. This proposal would have no impact on the BAP.

Officials of the **Department of Higher Education (DHE)** assume this proposal would have no impact on their agency. However, DHE is concerned about the creation of a parallel board system to that which already exists for the MO$T program. The new board creates potential conflicts of interest for the board members. The DHE is also concerned that the investment in a parallel system may be less effective at increasing higher education participation than programs focused specifically on lower and middle-income families. In addition, DHE assumes potential reductions to General Revenue could result in reduced funding to higher education institutions.

Officials of the **State Auditor's Office (SAO)** assume an audit of this program would require at least 750 audit staff hours. SAO states that this is the average amount of time needed to audit a program of this size. SAO requests .5 FTE for this program.

Oversight assumes SAO can complete the required program audit with existing resources.

Officials of the **State Treasurer's Office (STO)** assume there are 2 main objectives to this proposal. The first objective of this proposal is to extend a Missouri State income tax deduction to all 529 programs. Current law limits the deduction only for contributions to Missouri's 529 savings program (MO$T). The second objective of this proposal is to establish a "deposit program" overseen by a second board. STO assumes it is not possible to firmly predict the economic effects this second program would have on the state. However, STO has estimated the economic impact with this part of the proposal.

STO assumes, with the passage of this proposal, broker-dealers throughout the state would be offering 529 plans from all states, and thus Missouri contributions to these programs would increase significantly. In addition to the growth in participation, STO assumes that brokers would market these 529 plans to individuals at higher income levels. Factors such as an increase in participation, an increase in the average level of contributions, and interest earnings that grow tax free at the state level, would result in a significant amount of revenue being shielded from state income tax.

STO fiscal note calculations are based upon projected contributions to the MO$T program and estimated projections of participation in other 529 programs. While the STO can more accurately predict growth to the MO$T program, estimations as to Missourians' participation in other 529 programs are provided in a range due to variable future economic and business factors. Projections and estimations have been extrapolated from historical data and actuarial predictions.

ASSUMPTION (continued)

STO noted that an advisor series program was launched by the Missouri Saving for Tuition Program a few weeks ago and at this time, it is impossible for STO to predict its impact.

STO assumes it is impossible to predict the impact of expanding the Missouri tax deduction to all 529 plans with absolute certainty. Therefore, the STO has provided a range for estimating fiscal impact. The lower end of this range is based upon a very conservative number of broker-dealer customers investing in other 529 programs. The higher end of this range is based upon a higher number of broker-dealer customers investing rather moderately in other 529 programs. The STO anticipates the actual figure will be somewhere in-between, but nearer the higher end of the range.

STO estimates the revenue loss to the state of Missouri may be as little as $12.8 million in **2004** but is likely to be much higher, as much as $27.4 million. 529 program data is compiled based on tax years (calendar years) rather than fiscal years. As such, this worksheet shows figures based on calendar years.

2004 Estimated Calculations:

Lower Range
$303.33 million in tax deductible contributions to other 529 plans will result in a $18.2 million loss in state tax revenue.
[$303.33 million x 6% Missouri tax rate = $18.2 million tax loss.]

The MO$T program anticipates about $90.1 million in tax deductible contributions in 2004, which will result in a $5.4 million loss in state revenue. [$90.1 million x 6% MO tax rate = $5.4 million tax loss.]

The resulting fiscal impact [$18.2 million less $5.4 million = $12.8 million] will be a loss to General Revenue of approximately $12.8 million.

Higher Range
$546.66 million in tax deductible contributions to other 529 plans will result in a $32.8 million loss in state tax revenue.
[$546.66 million x 6% Missouri tax rate = $32.8 million tax loss.]

The MO$T program anticipates about $90.1 million in tax deductible contributions in 2004, which will result in a $5.4 million loss in state revenue. [$90.1 million x 6% MO tax rate = $5.4 million tax loss.]

ASSUMPTION (continued)

The resulting fiscal impact [$32.8 million less $5.4 million = $27.4 million] will be a loss to General Revenue of approximately $27.4 million.

STO estimates revenue loss to the state of Missouri may be as little as $16.5 million in **2005** but is likely to be much higher, as much as $33.6 million. 529 program data is compiled based on tax years (calendar years) rather than fiscal years. As such, this worksheet shows figures based on calendar years.

2005 Estimated Calculations:

Lower Range
$386.66 million in tax deductible contributions to other 529 plans will result in a $23.2 million loss in state tax revenue.
[$386.66 million x 6% Missouri tax rate = $23.2 million tax loss.]

The MO$T program anticipates about $111.66 million in tax deductible contributions in 2005, which will result in a $6.7 million loss in state revenue. [$111.66 million x 6% MO tax rate = $6.7 million tax loss.]

The resulting fiscal impact [$23.2 million less $6.7 million = $16.5 million] will be a loss to General Revenue of approximately $16.5 million.

Higher Range
$671.66 million in tax deductible contributions to other 529 plans will result in a $40.3 million loss in state tax revenue.
[$671.66 million x 6% Missouri tax rate = $40.3 million tax loss.]

The MO$T program anticipates about $111.66 million in tax deductible contributions in 2005, which will result in a $6.7 million loss in state revenue. [$111.66 million x 6% MO tax rate = $6.7 million tax loss.]

The resulting fiscal impact [$40.3 million less $6.7 million = $33.6 million] will be a loss to General Revenue of approximately $33.6 million.

STO assumes the revenue loss to the state of Missouri may be as little as $21.2 million in **2006** but is likely to be much higher, as much as $41.2 million. 529 program data is compiled based on tax years (calendar years) rather than fiscal years. As such, this worksheet shows figures based on calendar years.

ASSUMPTION (continued)

2006 Estimated Calculations:

Lower Range
$491.66 million in tax deductible contributions to other 529 plans will result in a $29.5 million loss in state tax revenue.
[$491.66 million x 6% Missouri tax rate = $29.5 million tax loss.]

The MO$T program anticipates about $138.33 million in tax deductible contributions in 2006, which will result in a $8.3 million loss in state revenue. [$138.33 million x 6% MO tax rate = $8.3 million tax loss.]

The resulting fiscal impact [$29.5 million less $8.3 million = $21.2 million] will be a loss to General Revenue of approximately $21.2 million.

Higher Range
$825 million in tax deductible contributions to other 529 plans will result in a $49.5 million loss in state tax revenue.
[$825 million x 6% Missouri tax rate = $49.5 million tax loss.]

The MO$T program anticipates about $138.33 million in tax deductible contributions in 2006, which will result in a $8.3 million loss in state revenue. [$138.33 million x 6% MO tax rate = $8.3 million tax loss.]

The resulting fiscal impact [$49.5 million less $8.3 million = $41.2 million] will be a loss to General Revenue of approximately $41.2 million.

In addition, STO assumes the Missouri Higher Education Deposit Program would have the following negative fiscal impact:

Fiscal year **2004**: $48 million in tax deductible contributions to the deposit program will result in a $2.88 million loss in state tax revenue.
[$48 million x 6% mo. Tax rate = $2.88 million tax loss.]

Fiscal year **2005**: $60 million in tax deductible contributions to the deposit program will result in a $3.60 million loss in state tax revenue.
[$60 million x 6% mo. Tax rate = $3.60 million tax loss.]

Fiscal year **2006**: $75 million in tax deductible contributions to the deposit program will result in a $4.5 million loss in state tax revenue.
[$75 million x 6% mo. Tax rate = $4.5 million tax loss.]

ASSUMPTION (continued)

STO's estimate for the fiscal impact of the deposit program assumes 12,000 accounts with an average contribution of $4,000 per account at a tax rate of 6%. Also, STO assumes 250 banks would participate in this program.

Oversight has, for fiscal note purposes only, changed the starting salary for two Tax Processing Technicians 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 for a six month period and the policy of the Oversight Subcommittee of the Joint Committee on Legislative Research.

According to the website for the College Savings Plans Network, all fifty states now offer Section 529 state college savings plans. Last year, the programs received federal tax exemption as part of the Economic Growth and Tax Relief Reconciliation Act of 2001. Oversight assumes with the significant tax incentives offered by the federal and state government, this program has the potential to attract more investors.

According to the website for the Federal Reserve Board the national savings rate for households in 2000 was 1.3 percent. Oversight assumes the estimate calculated by STO could be reduced to better reflect the actual savings rate of Missourians. However, Oversight has not been able to obtain information to better determine the percentage of growth for this program and will show the revenue impact of this proposal as a negative unknown, expected to exceed $100,000 annually.

This proposal will decrease Total State Revenue.

FISCAL IMPACT - State Government	FY 2004 (10 Mo.)	FY 2005	FY 2006
GENERAL REVENUE FUND			
Loss - General Revenue			
Increased contributions to higher ed savings progs.	(Unknown)	(Unknown)	(Unknown)
Deposit program	(Unknown)	(Unknown)	(Unknown)
Total Loss - GR	(Unknown)	(Unknown)	(Unknown)
Cost - Department of Revenue			
Personal Service (2 FTE)	($32,042)	($39,411)	($40,396)
Fringe Benefits	($12,967)	($15,950)	($16,348)

FISCAL IMPACT - State Government	FY 2004 (10 Mo.)	FY 2005	FY 2006
Equipment and Expense	($14,274)	($1,038)	($1,070)
Total Costs - DOR	($59,283)	($56,399)	($57,814)
TOTAL ESTIMATED NET EFFECT ON GENERAL REVENUE	**($59,283 to Unknown)**	**($56,399 to Unknown)**	**($57,814 to Unknown)**

FISCAL IMPACT - Local Government	FY 2004 (10 Mo.)	FY 2005	FY 2006
	$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 proposal enables an income tax deduction of up to $8,000 for an individual and up to $16,000 for a combined return for total annual contributions made to qualified savings programs and I.R.C. Section 529 plans. Current law only allows such deduction in the amount of $8,000, without specifying treatment of combined returns, and limits the deduction to only qualified savings program contributions. The bill also makes a technical change to clarify the tax status of certain 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

Department of Revenue
Office of Administration
   Budget and Planning
Department of Higher Education
State Treasurer
Office of the Governor

Mickey Wilson, CPA
Director
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