

COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 0976S.01I
Bill No.: SB 157
Subject: Taxation And Revenue - Income
Type: Original
Date: April 7, 2021

Bill Summary: This proposal modifies provisions relating to income tax exemptions for certain retirement benefits.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND			
FUND AFFECTED	FY 2022	FY 2023	FY 2024
General Revenue Fund		Less than (\$465,949,558) up to (\$666,954,087)	Less than (\$465,949,558) up to (\$666,954,087)
	\$0		
Total Estimated Net Effect on General Revenue		Less than (\$465,949,558) up to (\$666,954,087)	Less than (\$465,949,558) up to (\$666,954,087)
	\$0		

ESTIMATED NET EFFECT ON OTHER STATE FUNDS			
FUND AFFECTED	FY 2022	FY 2023	FY 2024
Total Estimated Net Effect on <u>Other</u> State Funds			
	\$0	\$0	\$0

Numbers within parentheses: () indicate costs or losses.

ESTIMATED NET EFFECT ON FEDERAL FUNDS			
FUND AFFECTED	FY 2022	FY 2023	FY 2024
Total Estimated Net Effect on <u>All</u> Federal Funds	\$0	\$0	\$0

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)			
FUND AFFECTED	FY 2022	FY 2023	FY 2024
Total Estimated Net Effect on FTE	0	0	0

☒ Estimated Net Effect (expenditures or reduced revenues) expected to exceed \$250,000 in any of the three fiscal years after implementation of the act or at full implementation of the act.

☐ Estimated Net Effect (savings or increased revenues) expected to exceed \$250,000 in any of the three fiscal years after implementation of the act or at full implementation of the act.

ESTIMATED NET EFFECT ON LOCAL FUNDS			
FUND AFFECTED	FY 2022	FY 2023	FY 2024
Local Government	\$0	\$0	\$0

FISCAL ANALYSIS

ASSUMPTION

Officials from the **Office of Administration – Budget & Planning Division (B&P)** state this proposed legislation will reduce Total State Revenue (TSR) by an amount up to \$641,800,000 annually once SB 509 (2014) has fully implemented.

Furthermore, B&P states this proposed legislation will impact the calculation under Article X, Section 18(e).

Section(s) 143.124 & 143.125 – Public Pension Exemption and Social Security Exemption

Officials from **B&P** state Section 143.124 would eliminate the income limits for the Individual Income Tax exemption for public pensions beginning with Tax Year 2022. Currently, taxpayers who file married filing combined may exempt 100% of their public pension income if their Missouri Adjusted Gross Income (MAGI) is equal to or less than \$100,000. All other taxpayers may exempt 100% of their public pension income if their MAGI is equal to or less than \$85,000.

Based on data published by the Internal Revenue Service (IRS), B&P estimates that this section may exempt up to \$1,718,479,222 in pension and annuity payments for taxpayers filing single, \$421,769,123 for taxpayers filing head of household, and \$7,584,208,806 for married filing joint taxpayers; for a total of up to \$9,724,457,151 in income exempted under this section. B&P notes that some of these pension and annuity payments may remain taxable, if they are not public pensions/annuities. Therefore, B&P will reflect the loss from this section as “up to”.

However, exemptions do not reduce revenues on a dollar for dollar basis, but rather in proportion to the top tax rate applied. Therefore, B&P will show the estimated impacts throughout the implementation of the tax rate reductions from SB 509 (2014). Consequently, B&P estimates that this section could reduce TSR and General Revenue (GR) by an amount up to \$525,120,686 (top tax rate 5.4%) or by up to \$515,396,229 (top tax rate 5.3%) in Fiscal Year 2023. Once SB 509 (2014) has fully implemented, this section could reduce TSR and GR by up to \$495,947,315 annually.

B&P states Section 143.125 would eliminate the income limits for the Individual Income Tax exemption for social security payments beginning with Tax Year 2022. Currently, taxpayers who are married filing combined may exempt 100% of their social security income, if their Missouri Adjusted Gross Income (MAGI) is equal to or less than \$100,000. All other taxpayers may exempt 100% of their social security income if their MAGI is equal to or less than \$85,000.

Based on data published by the IRS, B&P estimates that this section may exempt \$583,096,123 in social security payments for taxpayers filing single, \$145,362,364 for taxpayers filing head of household, and \$2,131,123,734 for married filing joint taxpayers; for a total of \$2,859,582,221 in income exempted under this section.

However, exemptions do not reduce revenues on a dollar for dollar basis, but rather in proportion to the top tax rate applied. Therefore, B&P will show the estimated impacts throughout the implementation of the tax rate reductions from SB 509 (2014).

B&P estimates that this section could reduce TSR and GR by \$154,417,440 (top tax rate 5.4%) or by \$151,557,858 (top tax rate 5.3%) in Fiscal Year 2023. Once SB 509 (2014) has fully implemented, this section could reduce TSR and GR by \$145,838,693 annually.

Officials from **B&P** estimate that this proposed legislation could reduce TSR and GR by an amount up to up to \$679,538,126 (top tax rate 5.4%) or by up to \$666,954,087 (top tax rate 5.3%) in Fiscal Year 2023. Once SB 509 (2014) has fully implemented, this proposed legislation could reduce TSR and GR by up to \$641,786,008 annually.

Retirement Income	Top Tax Rate			
	5.4%	5.3%	5.2%	5.1%
Pensions/Annuities	\$525,120,686	\$515,396,229	\$505,671,772	\$495,947,315
Social Security	\$154,417,440	\$151,557,858	\$148,698,275	\$145,838,693
Total GR Loss	\$679,538,126	\$666,954,087	\$654,370,047	\$641,786,008

Officials from the **Missouri Department of Revenue (DOR)** state, currently, a taxpayer may be subject to a portion of their social security benefits, military pension and/or their public pension benefits being taxable. The taxability is based on the taxpayer's filing status (single, head of household, or married filing combined) and their income level. This proposed legislation, beginning January 1, 2022, would exempt all these benefits regardless of the taxpayers filing status or income. DOR notes the returns for Tax Year 2022 would be filed starting in January 1, 2023.

Using IRS Individual Income Tax data and Tax Data for Tax Year 2018, DOR was able to estimate the projected loss to GR from this proposed legislation. The IRS collects data on the amount of pension and annuities money that are used in calculating AGI. DOR notes this amount does include both public and private pensions and well as military pensions. While this proposed legislation would exempt the military pension and public pensions, it does not include private pensions. Since DOR was unable to determine the amount of private pensions and exclude that money from the calculations, DOR notes the actual impact is expected to be less than the stated amount.

Tax Year	Current Law	TY22* / FY23	TY23 / FY24
Tax Rate	5.4%	5.3%	5.3%
Pensions/Annuities	(\$525,120,686)	(\$515,396,229)	(\$515,396,229)
Social Security	(\$154,417,440)	(\$151,557,858)	(\$151,557,858)
Total GR Loss	(\$679,538,126)	(\$666,954,087)	(\$666,954,087)

Oversight notes the data used by B&P and DOR include pensions from private sources. Therefore, Oversight assumes the estimates provided could be overestimated by an amount equal to the unknown amount of private pension(s) included.

Oversight notes, currently, Section 143.124.5 allows a taxpayer to claim an exemption equal to one hundred percent (100%) of the retirement benefits received from sources other than privately funded sources in the tax year, but not to exceed the maximum social security benefit available for such tax year. Moving forward, Oversight will refer to this exemption as the “Public Pension Exemption”.

Currently, a taxpayer shall be entitled to the Public Pension Exemption provided: (1) the taxpayer’s filing status is married filing combined, and their combined Missouri Adjusted Gross Income is equal to or less than one hundred thousand dollars (\$100,000); or (2) the taxpayer’s filing status is single, head of household, qualifying widow(er), or married filing separately, and the taxpayer’s Missouri Adjusted Gross Income is equal to or less than eighty-five thousand dollars (\$85,000).

Oversight notes, currently, pursuant to Section 143.124.6, if a taxpayer’s Missouri Adjusted Gross Income exceeds the aforementioned income ceilings, the Public Pension Exemption shall be reduced by one dollar (\$1) for every dollar the taxpayer’s income exceeds the aforementioned income ceilings.

Oversight notes the aforementioned language currently recognized in Section 143.124.5 would become obsolete under this proposed legislation for all tax years beginning on or after January 1, 2022.

Oversight notes this proposed legislation states, for all tax years beginning on or after January 1, 2022, taxpayers shall be entitled to the maximum Public Pension Exemption provided by this subsection regardless of the taxpayer’s filing status or the amount of the taxpayer’s Missouri Adjusted Gross Income.

Therefore, **Oversight** assumes this proposed legislation would exempt one hundred percent (100%) of the retirement benefits received by taxpayers from sources other than privately funded sources from Individual Income Tax for the tax year the retirement benefits are received.

Oversight assumes, then, since one hundred percent (100%) of the retirement benefits received by taxpayers from sources other than privately funded sources would become exempt from taxation, regardless of a taxpayer’s filing status or the amount of a taxpayer’s Missouri Adjusted

Gross Income, the amount of Public Pension Exemption recognized by some taxpayers could increase.

Oversight notes, per information provided to Oversight by the University of Missouri's Economic & Policy Research Analysis Center, in regards to similar legislation ([SB 847 – 2020](#)), public pension income is estimated to total approximately 61% of total pension income.

Therefore, **Oversight** estimates, using the same IRS data used by B&P and DOR, and applying the estimated percent attributable to public pensions specifically, the elimination of the income ceilings for the Public Pension Exemption could reduce GR by the following amount(s):

Tax Rate	5.40%	5.30%	5.20%	5.10%
Reduction To GR	(\$320,323,618)	(\$314,391,700)	(\$308,459,781)	(\$302,527,862)

However, **Oversight** notes, currently, Section 143.124.7 states the Public Pension Exemption shall be reduced by an amount equal any Social Security benefit exemption provided under Section 143.125. Oversight notes Section 143.124.7 is unchanged by this proposed legislation.

Therefore, **Oversight** assumes the provision of Section 143.124.7 would remain applicable to the Public Pension Exemption, as modified by this proposed legislation.

As a result of Section 143.124.7, **Oversight** assumes an increase in the Social Security Exemption could result in a lesser amount of Public Pension Exemption. Oversight notes this proposed legislation appears to allow for an increased Social Security Exemption (see below). Therefore, the estimated reduction to GR, as reported above, could be overestimated. **Oversight notes Section 143.124.7 would only impact taxpayers that receive both retirement benefits and social security benefits and whose Missouri Adjusted Gross Income exceeds the income ceilings currently in place.** Oversight is unable to determine the impact Section 143.124.7 will have on the estimated reduction to GR, as reported above.

Oversight notes, currently, Section 143.125 allows taxpayers to claim an exemption equal to one hundred percent (100%) of the social security benefits received in the tax year. Moving forward, Oversight will refer to this exemption as the “Social Security Exemption”.

Oversight notes, currently, the Social Security Exemption is bound by the same income ceilings as the Public Pension Exemption and the Social Security Exemption shall also be reduced by one dollar (\$1) for every dollar the taxpayer's income exceeds the income ceilings.

Oversight notes this proposed legislation also modifies the Social Security Exemption, in such that, for all tax years beginning on or after January 1, 2022, a taxpayer shall be entitled to the

maximum Social Security Exemption regardless of the taxpayer's filing status or the amount of the taxpayer's Missouri Adjusted Gross Income.

Therefore, **Oversight** assumes this proposed legislation would exempt one hundred percent (100%) of the social security benefits received by taxpayers from Individual Income Tax for the tax year the social security benefits are received.

Oversight assumes, then, since one hundred percent (100%) of the social security benefits received by taxpayers would become exempt from taxation, regardless of a taxpayer's filing status or the amount of a taxpayer's Missouri Adjusted Gross Income, the amount of Social Security Exemption recognized by some taxpayers could increase.

Oversight estimates, using the same IRS data used by B&P and DOR, the elimination of the income ceilings for the Social Security Exemption could reduce GR by the following amount(s):

Tax Rate	5.40%	5.30%	5.20%	5.10%
Reduction To GR	(\$154,417,440)	(\$151,557,858)	(\$148,698,275)	(\$145,838,693)

Oversight assumes, if the purpose of this proposed legislation is to fully exempt social security benefits, as written, social security benefits might be implicitly taxed; for each additional dollar recognized under the Social Security Exemption, as a result of this proposed legislation, the Public Pension could be further reduced by each dollar. Oversight assumes this would only be applicable to taxpayers that receive both retirement benefits and social security benefits whose Missouri Adjusted Gross Income exceeds the income ceilings currently in place.

Based on the information provided above, **Oversight** estimates this proposed legislation could reduce GR by the following amount(s):

Tax Rate	5.40%	5.30%	5.20%	5.10%
Reduction To GR	(\$474,741,058)	(\$465,949,557)	(\$457,158,056)	(\$448,366,555)

Oversight assumes Oversight's estimate(s) could be overestimated since Oversight is unable to determine the actual and true amount of pension income that is from public sources vs. the actual and true amount of pension income that is from private sources.

In addition, Oversight's estimates could be overestimated since Oversight is unable to determine the impact the increase in Social Security Exemption will have on the Public Pension Exemption.

Oversight notes the current top Individual Income Tax rate is subject to be reduced by one-tenth of one percent (0.1%) three (3) more times pursuant to SB 509 (2014). A reduction in the top rate of tax shall only occur if the amount of net general revenue collected in the previous fiscal year exceeds the highest amount of net general revenue collected in any of the three fiscal years prior to such fiscal year by at least \$150 million.

The current top Individual Income Tax rate for Tax Year 2021 is 5.4%.

Oversight anticipates the top Individual Income Tax rate will be reduced from 5.4% to 5.3% for Tax Year 2022. This assumption is partly based on the extended tax filing due date for Tax Year 2019 which pushed some revenues that would have normally be recognized in Fiscal Year 2020 into Fiscal Year 2021.

Once the top tax rate is reduced from 5.4% to 5.3%, two (2) more rate reductions could occur, in future, but separate, tax years, pursuant to SB 509 (2014).

Oversight does not anticipate the top rate of tax to reduce in Tax Year 2023 (Fiscal Year 2024). Therefore, for purposes of this fiscal note, Oversight will report the revenue reduction assuming the top Individual Income Tax rate is 5.3%.

For purposes of this fiscal note, **Oversight** will report a revenue reduction to GR, as a result of the modifications to the Public Pension Exemption, equal to a range, beginning with an amount “Less Than” (taking into consideration the assumption that the estimate(s) are overstated) Oversight’s estimate when using a top rate of tax equal to 5.3%, “Up To” B&P’s and DOR’s estimate when using a top rate of tax equal to 5.3%.

For purposes of this fiscal note, **Oversight** will report a revenue reduction to GR, as a result of the modifications to the Social Security Exemption equal to an amount “Up To” the amount(s) estimated by B&P, DOR, and Oversight

Oversight notes the provisions of this proposed legislation would begin for all tax years beginning on or after January 1, 2022. Oversight notes taxpayers will not file their Tax Year 2022 tax return until after January 1, 2023 (Fiscal Year 2023). Therefore, Oversight will report the aforementioned impact(s) beginning in Fiscal Year 2023.

<u>FISCAL IMPACT – State Government</u>	FY 2022 (10 Mo.)	FY 2023	FY 2024
GENERAL REVENUE FUND			
<u>Revenue Reduction – Section 143.124 – Elimination Of Income Ceilings From Public Pension Exemption Calculation</u>	\$0	Less than (\$314,391,700) up to (\$515,396,229)	Less than (\$314,391,700) up to (\$515,396,229)
<u>Revenue Reduction – Section 143.125 – Elimination of Income Ceilings From Social Security Exemption Calculation</u>	\$0	Up to (\$151,557,858)	Up to (\$151,557,858)
ESTIMATED NET EFFECT ON GENERAL REVENUE FUND	<u>\$0</u>	<u>Less than (\$465,949,558) up to (\$666,954,087)</u>	<u>Less than (\$465,949,558) up to (\$666,954,087)</u>

<u>FISCAL IMPACT – Local Government</u>	FY 2022 (10 Mo.)	FY 2023	FY 2024
	<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.

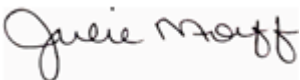
FISCAL DESCRIPTION

Current law allows taxpayers with certain filing status and adjusted gross income below certain thresholds to deduct 100% of certain retirement and Social Security benefits from the taxpayer's Missouri adjusted gross income, with a reduced deduction as the taxpayer's adjusted gross income increases. For all tax years beginning on or after January 1, 2022, this act allows the maximum deduction to all taxpayers regardless of filing status or adjusted gross income.

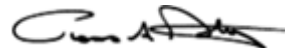
This legislation is not federally mandated, would not duplicate any other program and would not require additional capital improvements or rental space.

SOURCES OF INFORMATION

Office of Administration – Budget & Planning Division
Missouri Department of Revenue



Julie Morff
Director
April 7, 2021



Ross Strobe
Assistant Director
April 7, 2021