MISSOURI BUDGET PROJECT

# HB 548 Would Further Destabilize MO Budget

Although certain provisions of House Committee Substitute for House Bill 548 (HB 548) would close an ongoing tax loophole, the remainder of the bill would make Missouri's tax structure more unfair for most Missourians, shortchange education funding, and jeopardize the resources our communities need to prosper. The bill would cost Missouri $74 million in just the first full tax year of implementation.

The House Committee Substitute for House Bill 548 (HB 548) would:

- Implement the components of the **"Wayfair Fix,"** allowing Missouri to collect sales taxes owed on online retail purchases just like the state does for purchases at local retailers.[1]
- **Endanger public services while directing an additional tax cut to Missouri's wealthiest.** The bill would cut the top rate of income tax by 0.14 in the first year of implementation, followed by additional reductions in the income tax rate that would be triggered by growth in sales tax revenue.
- **Shortchange pre-K to 12 education funding by diverting currently earmarked sales taxes for education**. Earmarked sales taxes that would be collected under the "Wayfair Fix" would be designated as general revenue, reducing education funding over time as e-commerce grows.
- **Limit the ability of cities and counties to collect taxes due for online retail purchases,** even if those localities already have a "use tax."

A recent analysis conducted by the Institute on Taxation and Economic Policy (ITEP) found that for each 0.1 point reduction in the top rate of individual income tax, Missouri would lose $117 million in state general revenue for services per year. Using this as a base to calculate the initial impact of HB 548, **MBP estimates that HB 548 would cut state income tax revenue by $164 million per year beginning in the first full year of implementation.**

**HCS HB 548 – Impact on State General Revenue**
First full year of Implementation

Not Including Additional "Triggered" Reductions in Income Tax Rate

| | |
|---|---|
| State General Revenue Sales Tax (current 3% rate) | $67.32 million |
| Diversion of State Earmarked Sales Tax for Schools (current 1% rate) | $22.45 million |
| Subtotal Sales Tax for General Revenue | $89.77 million |
| Income Tax – Top Rate Reduction of 0.14 | ($164 million) |
| Combined Impact on General Revenue | ($74.23 million) |

# HB 548 Would Make Missouri's Tax Structure More Regressive

**Eighty percent of Missourians would see $40 or less per year from HB 548. A full sixty percent of Missourians would get just $18 per year or less. But the $164 million lost to our state could:**

- Fund payments on the Governor's transportation bonding proposal, helping to fix our roads and bridges and increase the safety of our transportation infrastructure; or
- Increase funding for local schools, making new investments in pre-k education, teacher salaries, and restoring school transportation funding that's been cut in recent years; or
- Increase investments in workforce development and higher education, preparing young adults for success in a changing economy; or
- Restore funding for critical investments in health and mental health for children, seniors and families, laying the foundation for families and communities to thrive.

While all Missourians would bear the consequences of reductions in funding for the services our communities need to create a thriving environment, the income tax change would increase the regressive design of Missouri's tax structure – making it less fair than the current structure.

In fact, while most Missourians would see little income tax reduction, the wealthiest Missourians would get $1,523 per year. This reduction would come on top of multiple changes in the state tax code in recent years that are similarly designed to benefit the wealthiest Missourians.

**Impact of Reducing the Top Rate of Income Tax by 0.14**

*Based on Calculations from the Institute on Taxation & Economic Policy – February 2019*

| 2019 Income | Lowest 20% | Second 20% | Middle 20% | Fourth 20% | Next 15% | Next 4% | Top 1% |
|---|---|---|---|---|---|---|---|
| **Income Range** | Less than $22,000 | $22,000 – $39,000 | $39,000 – $62,000 | $62,000 – $101,000 | $101,000 – $206,000 | $206,000 – $485,000 | $485,000 or more |
| **Average Income in Group** | $13,000 | $29,000 | $49,000 | $80,000 | $137,000 | $295,000 | $1,372,000 |
| **Average Tax Change ($)** | –0 | –4 | –18 | –40 | –112 | –288 | –1,523 |

# House Bill 548 Would Divert Funding Away from Pre-K to 12 Education & Missouri Communities

HB 548 would implement the "Wayfair Fix" and enable Missouri to collect sales taxes owed on online retail purchases the same way it does for purchases from local retailers. However, **it would divert the earmarked portion of sales taxes collected on online purchases to the state general revenue fund instead of the intended purposes, such as education.**

- The bill would apply the state sales tax rate of 4.225 percent to online retail purchases.
- Currently 1.225 of that rate is earmarked for specific needs, with 1 point of the state sales tax rate supporting local schools and .225 point of the state sales tax rate benefiting conservation, natural resources and parks.
- HB 548 attempts to divert all of those earmarked sales tax revenues to state general revenue. The bill further attempts to divert the motor vehicle sales tax to general revenue.

## Voter-Approved Education Funding Could Be Redirected

Missouri's sales taxes for conservation, natural resources and parks, and motor vehicles are all constitutionally restricted and revenues from those taxes are therefore prohibited from being sent to the general revenue fund.

However, education sales tax revenue is not constitutionally protected and could be diverted as proposed in HB 548. Nevertheless, diverting thouse funds would completely undermine voters' intent when they approved the "Proposition C" sales tax for education in the 1980s. Moreover, as e-commerce is projected to grow over time, the impact of the sales tax diversion away from public schools would grow over time as well.

## Proposal Would Exclude Cities & Counties From Collecting Sales Taxes on Online Purchases

HB 548 would limit the ability of localities to collect taxes due for online retail purchases, even if those localities already have a "use tax." The bill only applies the statewide sales tax rate to online retail purchases. What's more, the bill actually **prohibits any additional state or local sales or use taxes from being applied to those purchases.**

As a result, cities and counties that rely on local sales taxes to fund services like public safety, fire, ambulance districts, children's or senior's services and mental health funds would be prohibited from collecting local sales taxes for online retail purchases. Localities could miss out on $85 million in revenue per year initially, but as e-commerce grows over time, the impact on localities will be more severe.

# APPENDIX: Estimating the Budget Impact of HB 548

## Calculating the Wayfair Fix:

In their June 2018 ruling on Wayfair vs. South Dakota, the U.S. Supreme Court determined that states can compel the collection of state and local sales taxes from remote sellers. The ruling not only incentivized policymakers to consider mechanisms that would allow Missouri to collect the taxes, but also led some to view the revenue as a potential "windfall" for the state.

However, there is no definitive analysis of the amount of state and local sales tax revenue that could result from collection of sales taxes from online retailers. A wide variety of estimates of the impact for states have been produced over the last decade.

The most recent was produced by the U.S. Government Accountability Office (GAO) in November of 2017.[2] The GAO report recognized that a large portion of online retailers are likely already compelled to collect the tax in most states due to maintaining physical locations in the states. Because of this, and like previous studies, the GAO produced both a "high" and "low" estimate of potential state and local sales tax collections for each state.[3]

Because Amazon already implemented collection of state sales taxes in Missouri, the Missouri Budget Project (MBP) utilized the GAO's "low" estimate of the potential impact on Missouri in order to assess recent state legislative proposals. In addition, the GAO estimate includes both state and local sales tax revenue. In the following table, MBP has divided the revenue estimate into categories (state general revenue, state earmarked revenue and local revenue) based on the portion of the total average state and local sales tax in Missouri that each comprise.

| Potential State and Local Sales Tax Revenue for Missouri Resulting from Compelling Online Retail Collections | |
|---|---|
| **State General Revenue (3% rate)** | **$67.32 million** |
| **State Earmarked Revenue (1.225% rate)** | **$27.45 million** |
| **Local Revenue (3.805% average rate)** | **$85.23 million** |
| **TOTAL State and Local (8.03% combined average rate)** | **$180 million** |

*These amounts reflect what Missouri could gain in the first full year of implementation, using the GAO's low estimate of the impact for Missouri. They are not adjusted for other factors, such as exemptions in Missouri's sales tax base. They are also not adjusted for the diversion of earmarked sales taxes as required in HB 548.*

## Calculating the Impact of Income Tax Changes:

MBP relies on the expertise of Institute on Taxation and Economic Policy (ITEP) for analyses of the impact of state tax law changes. ITEP conducts rigorous analyses of tax proposals at both the state and federal level using a Microsimulation Tax Model. The model is unique in its ability to produce analysis at the federal and state levels and to analyze income, consumption and property taxes. The model is known for its accuracy because it relies on one of the largest databases of tax returns and supplementary data in existence, created by the Internal Revenue Service. The ITEP model's federal tax calculations are similar to those produced by the congressional Joint Committee on Taxation, the U.S. Treasury Department and the Congressional Budget Office. The ITEP model, however, can be used to model both federal and state policies on a state-by-state basis, which is a capability not found in government models.

Using their microsimulation tax model, ITEP estimates that a 0.1 point reduction in the top rate of Missouri's income tax will cost $117 million. MBP relies on this estimate to assess the tax changes proposed in HB 548. Multiplying $117 million by 1.4 to determine the impact of a 0.14 reduction in the top rate of income tax, MBP finds that the income tax cut in HB 548 would result in a loss of $164 million annually.

It's important to note that this estimate of is not further adjusted for the additional cuts that would be triggered under HB 548. The bill requires that the top rate of income tax be reduced by an additional 0.05 points when sales tax revenue grows by $40 million and 4% in a year. If triggered, each additional reduction in income tax would result in an additional loss of $58 million in income tax revenue. MBP did not calculate these changes because the trigger proposal is unclear. The bill doesn't identify whether the trigger would be measured by the growth of the "Wayfair Fix" sales tax collections or the "Wayfair Fix" revenue and the existing sales tax. Nor does it specify whether the growth formula would be applied to general revenue sales taxes, all state sales taxes, or all state and local sales taxes.

## NOTES

1. See Wayfair Fix Can Help Stabilize Missouri's Budget, April 2, 2019, Missouri Budget Project at: http://www.mobudget.org/wayfair-fix-can-help-stabilize-missouris-budget/

2. United States Government Accountability Office (GAO), "SALES TAXES: States Could Gain Revenue from Expanded Authority, but Businesses Are Likely to Experience Compliance Costs", November 2017

3. The GAO's low estimate for Missouri was $180 million, while the high estimate was $275 million.