



GOVERNOR'S OFFICE OF
BUDGET AND PROGRAM PLANNING

Fiscal Note 2021 Biennium

Bill # HB0742

Title: Revise individual income tax and reduce school property taxes

Primary Sponsor: Woods, Tom

Status: As Introduced

- Significant Local Gov Impact
 Needs to be included in HB 2
 Technical Concerns
 Included in the Executive Budget
 Significant Long-Term Impacts
 Dedicated Revenue Form Attached

FISCAL SUMMARY

	<u>FY 2020</u> <u>Difference</u>	<u>FY 2021</u> <u>Difference</u>	<u>FY 2022</u> <u>Difference</u>	<u>FY 2023</u> <u>Difference</u>
Expenditures:				
General Fund	\$24,798,221	\$89,085,408	\$80,009,542	\$81,149,959
Revenue:				
General Fund	\$26,947,000	\$140,975,000	\$47,965,000	\$58,045,000
Net Impact-General Fund Balance:	<u>\$2,148,779</u>	<u>\$51,889,592</u>	<u>(\$32,044,542)</u>	<u>(\$23,104,959)</u>

Description of fiscal impact: HB 742 revises income tax laws to reduce property taxes which fund Montana state public education. HB 742 also increases the income phaseout of taxable social security income and further modifies personal income tax by adding rates and new tax brackets rates. The bill also reduces the state's equalization levy from 40 mills to 10 mills.

FISCAL ANALYSIS

Assumptions:

Department of Revenue (DOR)

Changes to the Taxation of Social Security Income

- Under current law, individuals with social security income can exempt a portion of that income from taxation when filing their Montana income tax. The exemption base amount is \$25,000 for individuals filing a single or head of household income tax return. For married individuals, the income exemption amount is \$32,000 if filing a joint return and \$16,000 if filing on separate returns.
- HB 742 changes the exemption base amount for Montana's income tax to \$30,000 for individuals filing a single or head of household return, \$60,000 for taxpayers filing a joint return and \$20,000 for individuals with a married filing separately return. The proposed bill also changes the definition of adjusted gross income to

include or exclude (depending on the income above or below the threshold), social security income that is now taxable income relative to federal taxable social security income.

Changes to Income Tax Rates and Brackets

- HB 742 also changes the rate at which all income is taxed. Under current law, Montana’s personal income tax rate increases as taxable incomes increase, with seven different tax rates and applicable brackets. The number of tax rates and their respective brackets increase under HB 742 to ten. A breakdown of the new tax rates and their tax brackets in HB 742 are provided in the table below.

Marginal Tax Rate Income Limits in TY 2020			
Current Law		HB 742	
Tax Rate	Income Limit	Tax Rate	Income Limit
1.0%	\$3,100	1.0%	\$3,500
2.0%	\$5,500	2.0%	\$6,900
3.0%	\$8,500	3.0%	\$14,000
4.0%	\$11,400	4.0%	\$20,900
5.0%	\$14,600	5.5%	\$28,000
6.0%	\$18,900	6.5%	\$34,900
6.9%	Unlimited	7.5%	\$48,900
		8.5%	\$69,800
		9.5%	\$122,100
		10.5%	Unlimited

- The changes made to personal income taxes apply starting tax year (TY) 2020.
- The HJ 2 income tax model was modified to include the changes made by HB 742. The tax liability of full-year resident taxpayers after the capital gains tax credit were estimated under current law and under the proposed bill. For TY 2020, HB 742 would increase the income tax liability of the taxpayers by \$133.049 million. For TY 2021, TY 2022 and TY 2023, tax liabilities increase to \$137.569 million, \$148.946 million and \$161.547 million respectively.
- The proposed changes will result in some taxpayers changing their withholding and estimated payments. The department would issue new withholding schedules to adjust for the tax changes. It is assumed that 20% of income tax liabilities will be collected during the same fiscal year as the tax year. The remaining 80% will be collected the following fiscal year.
- After adjusting for changes in withholding, estimated payments, non-resident taxpayers, and credits, the proposed bill would increase personal income tax revenue by \$26.947 in FY 2020, \$140.975 million in FY 2021, \$147.122 million in FY 2022 and \$159.346 million in FY 2023.

Changes to Statewide Property Tax Levies

- HB 742 changes the state equalization aid levy. Under current law, the state imposes a 40 mill levy on all taxable property in the state. HB 742 changes the mill levy from 40 mills to 10 mills. The changes apply to property tax years beginning after December 31, 2020.
- Assessed values are measured at the beginning of the calendar year, but not due to the state until the following November and May. That is, the tax is not collected until the following fiscal year.
- As the mill changes in HB 742 first apply to TY 2021, the impact to state general fund revenue will not begin until FY 2022.
- The assumptions used for HJ 2 estimate that the state’s 40 mill levy will generate \$132.209 million in revenue for FY 2022 and \$135.068 million in FY 2023.
- Based on the estimated 40 mill revenue estimates, the 10 mills set under HB 742 will generate \$33.052 million in revenue for FY 2022 and \$33.767 million in FY 2023.

13. The proposed change in the state’s equalization aid levy will reduce general fund revenue by \$99.157 million in FY 2022 and \$101.301 million in FY 2023.
14. When the proposed changes to the state’s personal income tax are combined with the changes to the state’s equalization aid levy, HB 742 will increase general fund revenue by \$26.947 million in FY 2020, \$140.975 million in FY 2021, \$47.965 million in FY 2022 and \$58.045 million in FY 2023.
15. The department does not expect significant costs because of the proposed bill.

Office of Public Instruction (OPI)

16. HB 742 revises income tax laws, reduces 40 school equalization mills to 10 mills, and revises state school funding.
17. Section 4 changes the guaranteed tax base aid (GTB) ratio multiplier to 341% from 232% beginning in FY 2021 and succeeding years. This change would cost the state an additional \$45 million per year beginning in FY 2021. A school district with a lower than percentage modified statewide average taxable value per ANB may qualify to receive a GTB tax subsidy. The increased ratio multiplier inflates the tax subsidy for school districts’ general fund. The following table shows the estimated changes to GTB.

	FY 2020	FY 2021	FY 2022	FY 2023
GF GTB Current Est. @ 232%	\$226,453,575	\$236,014,670	\$240,274,640	\$245,369,977
GF GTB Current Est. @ 341%	<u>\$226,453,575</u>	<u>\$280,181,404</u>	<u>\$285,155,730</u>	<u>\$291,179,519</u>
GF GTB Increase	\$0	\$44,166,734	\$44,881,090	\$45,809,542

18. Section 4 changes the multiplier for the school retirement GTB calculation from 121% in FY 2020 to 153% beginning in FY 2021 and succeeding years. Counties with a lower than percentage modified statewide average taxable value per county ANB may qualify to receive a retirement GTB tax subsidy. This would increase state retirement GTB tax subsidy paid to counties for school district retirement funds.
19. The OPI estimates county retirement GTB would increase by approximately \$20.1 million beginning in FY 2021. For purposes of this fiscal note, a 4.26% increase is assumed for retirement GTB years following.
20. HB 742 modifies 20-10-141, MCA, the schedule of maximum reimbursement by mileage rates for pupil transportation. Current reimbursement to school districts for pupil transportation is based on a mileage-per-day schedule where rates are determined on maximum bus capacity of seating positions. The current rates schedule and the HB 742 proposal, which increases each rate by \$0.90, are as follows:

Seating Positions	Rate per	Rate per
20-10-101(4)(a)(ii)	Current Law	HB 742
<= 10	\$0.50	\$1.40
0-49	\$0.95	\$1.85
50-59	\$1.15	\$2.05
60-69	\$1.36	\$2.26
70-79	\$1.57	\$2.47
80 or greater	\$1.80	\$2.70
Non-bus miles	\$0.50	\$1.40

21. Reimbursements calculated for pupil transportation based on this schedule currently are split so that half of the reimbursement is distributed through state payments and the remainder is paid through county reimbursement. HB 742 proposes to modify 20-10-144 and 20-10-146, MCA, so that the reimbursement percentage is 70% state payment and 30% county payment.
22. The OPI estimates that approximately 2,373 routes are claimed in total annually for reimbursement with 16.5 million annual miles claimed.

23. Current state distributions for pupil transportation claims are approximately \$12.0 million with an equal county distribution of \$12.0 million. The OPI estimates that the increase of rates will increase the maximum reimbursement by \$14.8 million making the total payment from state and county \$38.8 million.
24. Modification of the percentage paid by the state and counties would increase the state payments by \$15.2 million and reduce the county payments by \$0.4 million.
25. Districts may permissively levy property taxes to subsidize the reimbursements determined in 20-10-141, MCA. Based on the statewide report titled OPI Budget, in FY 2019 local property tax support of district transportation budget is \$63.2 million in addition to the schedule of reimbursements. The OPI assumes that the proposed increases will lower current levies supporting the transportation fund.
26. HB 742 appropriates \$10 million for school facility reimbursement in HB 2 for FY 2020 and for FY 2021. It is unclear the fund type appropriated. For purposes of this fiscal note it is assumed the bill intended general fund and \$10 million per year.

	<u>FY 2020</u> <u>Difference</u>	<u>FY 2021</u> <u>Difference</u>	<u>FY 2022</u> <u>Difference</u>	<u>FY 2023</u> <u>Difference</u>
<u>Fiscal Impact:</u>				
<u>Expenditures:</u>				
Local Assistance (GTB)	\$0	\$44,166,734	\$44,881,090	\$45,809,542
Local Assist (Retirement GTB)	\$0	\$20,120,453	\$20,330,231	\$20,542,196
Local Assist (Debt Service Assist GTB)	\$10,000,000	\$10,000,000	\$0	\$0
Local Assist (Transportation)	\$14,798,221	\$14,798,221	\$14,798,221	\$14,798,221
TOTAL Expenditures	<u>\$24,798,221</u>	<u>\$89,085,408</u>	<u>\$80,009,542</u>	<u>\$81,149,959</u>
<u>Funding of Expenditures:</u>				
General Fund (01)	\$24,798,221	\$89,085,408	\$80,009,542	\$81,149,959
TOTAL Funding of Exp.	<u>\$24,798,221</u>	<u>\$89,085,408</u>	<u>\$80,009,542</u>	<u>\$81,149,959</u>
<u>Revenues:</u>				
General Fund (01)	\$26,947,000	\$140,975,000	\$47,965,000	\$58,045,000
TOTAL Revenues	<u>\$26,947,000</u>	<u>\$140,975,000</u>	<u>\$47,965,000</u>	<u>\$58,045,000</u>
<u>Net Impact to Fund Balance (Revenue minus Funding of Expenditures):</u>				
General Fund (01)	\$2,148,779	\$51,889,592	(\$32,044,542)	(\$23,104,959)

Effect on County or Other Local Revenues or Expenditures:

Office of Public Instruction

1. The local property tax impact related to the general fund GTB inflator increase could reduce local property taxes by \$44 million in FY 2021 and ongoing.
2. The local property tax impact related to the retirement GTB inflator increase could reduce local property taxes by \$20 million in FY 2021 and ongoing.
3. The local property tax impact related to debt assistance GTB (school facility reimbursement) appropriation could reduce local property taxes by \$20 million over the 2021 biennium.
4. The local property tax impact related to increases in the pupil transportation maximum reimbursement schedule could reduce local property taxes by \$17.7 million beginning in FY 2020 and ongoing.

Technical Notes:

1. Section 10 of HB 742 appropriates \$10 million each year of the 2021 biennium for school facility reimbursement in HB 2. The fund type intended for this purpose is not clear. Currently, school facility reimbursement is paid from a state special revenue fund.

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<i>Sponsor's Initials</i>	<i>Date</i>	<i>Budget Director's Initials</i>	<i>Date</i>

TL

3/29/19