



GOVERNOR'S OFFICE OF
BUDGET AND PROGRAM PLANNING

Fiscal Note 2023 Biennium

Bill # SB0399

Title: Generally revise and simplify income taxes

Primary Sponsor: Hertz, Greg

Status: As Amended in Senate Committee

- 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 2022</u> <u>Difference</u>	<u>FY 2023</u> <u>Difference</u>	<u>FY 2024</u> <u>Difference</u>	<u>FY 2025</u> <u>Difference</u>
Expenditures:				
General Fund	\$0	(\$250,367)	(\$702,410)	(\$711,518)
Revenue:				
General Fund	(\$17,224,000)	(\$33,363,000)	(\$37,822,000)	(\$41,916,000)
Net Impact-General Fund Balance:	<u>(\$17,224,000)</u>	<u>(\$33,112,633)</u>	<u>(\$37,119,590)</u>	<u>(\$41,204,482)</u>

Description of fiscal impact: SB 399 as amended, changes Montana's individual income tax. Montana Taxable Income (MTI) is based on Federal Taxable Income. The number of tax rates is reduced from seven to two. Several individual and corporate income tax credits are eliminated. The changes first apply starting tax year (TY) 2022. The amendments correct the inflation factor reference, restore the historic preservation credit and the business recycling and mobile home park capital gains exclusions.

FISCAL ANALYSIS

Assumptions:

Department of Revenue

- SB 399 as amended, makes changes to Montana's individual income tax, while also making changes that will impact the taxation of estates and trusts, and the state's corporate income tax.
- The House Taxation Committee amendments to SB 399 changed the inflation factor used to adjust the tax rates and elderly exemption amounts each year. They also change Montana taxable income to exclude income from the purchase of business-related recycled material and the capital gains associated with the sale of eligible mobile home parks.
- Under current law, taxpayers calculate their Montana Taxable Income (MTI) by applying income that is taxed in Montana, but not at the federal level, and by subtracting income from sources that are not taxed by the state.

Next, taxpayers subtract either the state’s standard deduction or claim itemized deductions. Finally, taxpayers reduce that income by applying their personal income exemption and any exemptions allowed for dependents. Taxpayers are allowed additional exemptions for being at least 65 years old, or if they are blind.

4. Under SB 399, taxpayers MTI is based on their Federal Taxable Income, with additional adjustments. These adjustments include a 30% deduction on net-long term capital gains, the addition of the federal Qualified Business Income (QBI) deduction, a \$5,500 income exemption for taxpayers at least 65 years old, and several other income additions and income subtractions.
5. Under current law, taxpayers with positive MTIs have their income taxed at seven different tax rates, with tax rates ranging between 1% and 6.9%. The same income thresholds apply to all filing types.
6. Under SB 399, taxpayers with taxable income will have their income taxed at two rates, 4.7% and 6.5%. The income thresholds under which taxpayers pay the 6.5% rate changes depending on the taxpayer’s filing status.
7. Under SB 399 taxpayers must choose the same filing status as they used when filing their federal income tax.
8. SB 399 eliminates the state’s capital gains income tax credit of 2% of capital gains income.
9. The proposed bill also makes several changes to the Montana Education Savings Program. The proposed bill expands the types of expenditures Education Savings Program funds can be used for without having to pay tax on the income from the fund. Taxpayers can spend ESP money on any cost covered in 26 U.S. Code 529. New expenses allowed under the proposed changes include K-12 tuition, certain expenses for registered apprenticeships, and repayment of student loans. Taxpayers are also able to exempt income used for a qualified tuition program.
10. It is assumed that the proposed changes to the state’s Montana Education Savings Program will increase the amount of income exempted from Montana’s personal income tax by 50%.
11. The changes made by SB 399 apply starting TY 2022.
12. The Department of Revenue’s income tax model was modified to include the changes made by the proposed bill. The estimated income tax liability amounts under the proposed law were then compared to current law income and tax liability forecasts.
13. Based on the department’s income tax model, the changes made by SB 399 would reduce the income tax liability of full-year resident taxpayers by \$32.347 million in TY 2022. For TY 2023, TY 2024, and TY 2025, the tax liability of residents would decrease by \$36.383 million, \$39.536 million, and \$43.710 million, respectively.

Tax Liability under Current Law and SB 399 as Amended			
Tax Year	Tax Liability (Millions)		
	Current Law	SB 399.02	Change in Revenue
2022	\$1,393.283	\$1,360.936	(\$32.347)
2023	\$1,452.144	\$1,415.761	(\$36.383)
2024	\$1,519.063	\$1,479.527	(\$39.536)
2025	\$1,596.083	\$1,552.373	(\$43.710)

14. The change in taxable income and tax rates will require the department to update its withholding tables at the beginning of TY 2022. The changes to withholding tables will result in reduced income tax collections at the start of TY 2022, which is the second half of FY 2022. It is assumed that half the tax liability impact of the proposed law for each tax year will occur in the second half of the current fiscal year and the second half will occur during the first half of the following fiscal year.
15. The tax liability amounts from the proposed tax changes were adjusted based on HJ 2 assumptions for non-full-year resident taxpayers, audit collections, population increases, and other changes.
16. Based on a 50/50 distribution of the tax liability change across fiscal years, and the adjustments used for HJ 2, the proposed bill will reduce income tax revenue by \$17.224 million in FY 2022, \$38.085 million in FY 2023, \$42.972 million in FY 2024, and \$47.348 million in FY 2025.
17. SB 399 also eliminates several personal and corporate income tax credits and deductions.