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Scaled-Down Version of Economic Development Bill: Cost to State Revenue Remains Significant *Legislature Considers HB1 (a Revised HB327)*

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When the Missouri House of Representatives passed HB327 at the end of the 2007 session in May, even the House leadership agreed that it was too costly. What had started as a relatively small adjustment of Missouri's Quality Jobs Program was expanded to include several tax credits that would have cost Missouri \$200 million annually when fully phased in.¹ The Senate passed the bill the House had approved without scaling back the fiscal impact to the state.

Governor Matt Blunt vetoed HB327 and has called a special session of the Legislature beginning August 20; a scaled-down version of HB327—now named HB1-- will be considered. The Governor said that he wanted a “clean” bill that expanded the Quality Jobs Program, one of his top priorities. However, HB1 contains 97 pages of special interest provisions that extend far beyond the Quality Jobs Program.

HB1 Strays from Original Intent of Quality Jobs Program

The Missouri Budget Project supports state programs, including tax incentives, that are designed to create new jobs that pay higher than average salaries and which include employer-sponsored health insurance. The enhancement of the Quality Job Act, at an additional cost of \$14 million annually (in the original House Bill 327) may be an acceptable investment.

However, HB 1 is no longer solely about improving the Quality Jobs Act. The “scaled down” version of the bill contains a number of tax provisions that increase the annual cost of the bill to \$73 million. As the following describes, Missouri's fiscal situation demands that all components of HB1 be carefully studied for their potential “cost-benefit” for Missouri. Some of the provisions may primarily benefit narrow special interests rather than promoting the broad stability of working families.

¹ Governor Matt Blunt, News Release on veto of House Bill 327, July 6, 2007

Following is an examination of HB1, including the Quality Jobs Program, and the implications for Missouri should the bill be approved in its entirety.

Quality Jobs Program: 2006 Results in Missouri

Missouri's Quality Jobs Program began in 2005 as a business tax incentive intended to spur new job development in Missouri. To qualify for a tax reduction, employers must create new jobs or prove that the program will prevent job loss. The jobs are required to pay a wage that equals or exceeds the county average wage and provide health benefits with the company paying at least 50% of the premium. For 2006 the statewide average county wage equaled \$37,379.²

Additionally, employers are required to create a certain number of new jobs within two years to qualify, ranging from 40 new jobs for small employers (20 for small employers in rural areas) to more than 100 for high impact businesses. In exchange, depending on the number of jobs and the level of the wage paid, employers are allowed to retain withholding tax for 3-5 years and in some cases a percentage of payroll or an additional tax credit.

The amount of state funding for the withholding provision of the Quality Jobs Program is not limited, while the tax credit incentive side is currently limited to \$12 million annually. The total 2006 cost to the state of all tax incentives in the Quality Jobs Program was \$103 million.³

According to MERIC, the Missouri Economic Research and Information Center, the program funded 99 projects in calendar year 2006. MERIC estimated the economic impact of these projects alone will result in 11,714 new jobs paying an average wage of \$53,054 per year in Missouri. MERIC's estimates assume that these jobs would not have been created without this program which may or may not be the case.

Main Provisions, Costs of Revised Economic Development Bill

Public policy decisions on any tax incentives, including the Quality Jobs Program, should be assessed as any other state-funded program: by the amount of public benefit the program provides versus its cost to state tax dollars. The original intent of House Bill 327 was to increase the amount of state resources dedicated to the tax credit side of the Quality Jobs Program by \$14 million annually. Given the current level of success of the Program, this may be a prudent investment for the state. The provisions that require the creation of new jobs that pay above average wages and provide health benefits to employees may be some of the strongest tax credit requirements in the nation.

² Missouri Department of Economic Development

³ MERIC – Missouri Economic Research and Information Center – Department of Economic Development – “Economic Impact of the Missouri Quality Jobs Program – 2006 Projects”.

However, while the Quality Jobs Program has proven to be a good return on investment, HB1 doesn't simply stop there. A primary concern of the Governor, when he vetoed HB 327, was the growing cost of the expanded HB 327 that included a plethora of tax credits beyond its primary purpose. Many of these items remain in the "new scaled down" HB1, including:

1. Distressed Areas Land Assemblage Credit - **General Revenue Loss \$10 million**
2. Qualified Beef Tax Credit - **General Revenue Loss \$3 million**
3. Film Production Tax Credit - **General Revenue Loss \$3 million**
4. Enhanced Enterprise Zone - **General Revenue Loss \$7 million**
5. Quality Jobs Act Enhancement - **General Revenue Loss \$28 million**
6. New Markets Qualified Equity Investment Tax Credit **No Revenue Impact until FY 2010; then the GR loss is estimated at \$15 million annually**

If the draft bill is passed in its current form, the resulting General Revenue losses for the next three years are:

FY 2008	\$51 million
FY 2009	\$62 million
FY 2010	\$73 million

Future Impact of Tax Expenditures Must Be Considered

As tax credits are real expenditures of limited state tax dollars, the public benefit of all of the components of the Economic Development bill must be assessed for their cost and benefit to all Missourians. Legislators have a responsibility to balance the needs of one program with the needs of others. Thus, a new investment in job creation programs must be compared to new investments in other programs including education and health care.

This, however, is rarely acknowledged in debate about specific bills. The discussion usually proceeds as if tax credits have no impact on future budgets. However, given Missouri's critical revenue status, a review of the fiscal impact of the Economic Development Bill is critical.

The tables on the next pages provide a five-year General Revenue Summary and Outlook.⁴ As indicated, the first table projects the current budget outlook. Due to a combination of factors, including declining revenue growth and state tax cuts already passed in 2007, Missouri faces a shortfall of \$264 million by FY 2010. Official state estimates of Missouri's revenue situation concur. In a document prepared by the Senate Appropriations Staff during the 2007 legislative session, the Senate staff estimated that a \$100 million tax cut will result in a budget shortfall of \$83 million as quickly as Fiscal Year 2009, just one year from now.⁵

⁴ The numbers for Fiscal Year 2007 (FY 2007) are actual figures to date.

⁵ This document has not been broadly released, and was not directly provided by the Senate Appropriations Staff to the Missouri Budget Project. However, as an official state document, created by state staff and resources, it is subject to the State's "Sunshine Law". The documents are labeled "Confidential" and project only through Fiscal Year 2009.

If HB1 were to pass as written in the special session, the state budget situation becomes precarious following FY 2008. In FY 2009, the state would end the year with a revenue shortfall of about \$11.5 million and the FY 2010 budget would face a shortfall of nearly \$450 million.

These shortfalls are likely even though the FY 2007 net General Revenue collections exceeded the consensus forecast by about \$89 million. The state cannot afford additional erosion of the General Revenue tax base. State policy makers must pay attention to the long- term consequences of the tax cuts already enacted and exercise prudence before considering additional tax reductions presented in the special session.

Summary

The impact of the growing approval of tax credits, tax deductions, and tax exemptions on Missouri's revenue is a significant concern. The cumulative effect of allowing relatively small tax breaks to very narrow special interests makes it difficult to adequately fund what should be the state's priorities. Missouri has many unmet needs that require limited tax dollars. The state lags behind most other states in funding higher education, elementary and secondary education, health care and transportation (including road and bridge maintenance). The latest Morgan Quitno data show Missouri 44th in state general revenue spending per person, and 46th in state and local spending per capita.⁶ The already passed tax cuts cost the state more than \$100 million annually. Decreasing Missouri's general revenue by granting tax credits and other tax breaks exacerbates the situation.

The Missouri Budget Project is a statewide, nonprofit, nonpartisan fiscal analysis organization that informs the public on Missouri's budgetary and tax policy options...and their impact on low and middle income citizens. www.mobudget.org

⁶ Morgan Quitno State Rankings 2007

Table 1: Current Five Year Budget Outlook

Fiscal Year	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010
Resources					
Beginning Balance	\$185.6	\$600.6	\$605.2	\$407.1	\$102.5
Previous Year's Lapse	\$114.7	\$94.7	\$147.3	\$111.6	\$116.1
Net General Revenue Collections	\$7,332.2	\$7,716.4	\$7,959.4	\$8,277.8	\$8,608.9
Telecomm Court Case Refunds	\$0.0	\$0.0	(\$40.0)	(\$60.0)	(\$60.0)
2007 Tax Cuts	\$0.0	\$0.0	(\$40.0)	(\$76.0)	(\$100.0)
Transfers	\$188.1	\$192.8	\$150.2	\$150.2	\$150.2
Total Resources Available	\$7,820.6	\$8,604.5	\$8,782.1	\$8,810.7	\$8,817.7
Obligations					
Base Operating Appropriations	\$7,138.7	\$7,721.7	\$8,212.9	\$8,206.0	\$8,543.0
Confirmed lapse/withholdings	(\$68.8)	\$0.0	\$0.0	\$0.0	\$0.0
Foundation Formula	\$0.0	\$0.0	\$0.0	\$108.3	\$112.6
Higher Ed	\$0.0	\$0.0	\$0.0	\$34.9	\$36.3
Pay plan	\$0.0	\$0.0	\$0.0	\$44.5	\$46.3
Medicaid & everything else (On-Going)	\$0.0	\$0.0	\$0.0	\$149.2	\$155.2
One-time spending	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Capital Improvements	\$32.7	\$73.7	\$72.1	\$75.3	\$78.7
Supplementals / Estimateds	\$117.4	\$203.9	\$90.0	\$90.0	\$110.0
Total Obligations	\$7,220.0	\$7,999.3	\$8,375.0	\$8,708.2	\$9,082.1
Ending Balance	\$600.6	\$605.2	\$407.1	\$102.5	(\$264.4)

Table 1: Revised Five Year Budget Outlook with Scaled Back HB 327

Fiscal Year	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010
<u>Resources</u>					
Beginning Balance	\$185.6	\$600.6	\$605.2	\$356.1	(\$11.5)
Previous Year's Lapse	\$114.7	\$94.7	\$147.3	\$111.6	\$116.1
Net GR Collections	\$7,332.2	\$7,716.4	\$7,959.4	\$8,277.8	\$8,608.9
Telecomm Court Case Refunds	\$0.0	\$0.0	(\$40.0)	(\$60.0)	(\$60.0)
2007 Tax Cuts with "Revised HB 327"	\$0.0	\$0.0	(\$91.0)	(\$139.0)	(\$173.0)
Transfers	\$188.1	\$192.8	\$150.2	\$150.2	\$150.2
Total Resources Available	\$7,820.6	\$8,604.5	\$8,731.1	\$8,696.7	\$8,630.7
<u>Obligations</u>					
Base Operating Appropriations	\$7,138.7	\$7,721.7	\$8,212.9	\$8,206.0	\$8,543.0
Confirmed lapse/withholdings	(\$68.8)	\$0.0	\$0.0	\$0.0	\$0.0
Foundation Formula	\$0.0	\$0.0	\$0.0	\$108.3	\$112.6
Higher Ed	\$0.0	\$0.0	\$0.0	\$34.9	\$36.3
Pay plan	\$0.0	\$0.0	\$0.0	\$44.5	\$46.3
Medicaid & everything else (On-Going)	\$0.0	\$0.0	\$0.0	\$149.2	\$155.2
One-time spending	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Capital Improvements	\$32.7	\$73.7	\$72.1	\$75.3	\$78.7
Supplementals /Estimateds	\$117.4	\$203.9	\$90.0	\$90.0	\$110.0
Total Obligations	\$7,220.0	\$7,999.3	\$8,375.0	\$8,708.2	\$9,082.1
Ending Balance	\$600.6	\$605.2	\$356.1	(\$11.5)	(\$451.4)