

**EXAMINING MISSOURI'S TAX SYSTEM:
Tax Expenditures—A First Step**

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Context for the Analysis

Missouri state finances are presently the subject of intense debate as the cumulative events of the past three years have adversely impacted state revenues. At this writing, the budget shortfall of hundreds of millions of dollars has given way to in excess of a billion dollars projected for FY04. There is no certainty that the "fiscal bottom" has yet been reached. The national and state economies continue to flounder. Uncertainty undermines decisions by consumers to spend or not spend and on what and how much. Business decisions to invest, hire workers, innovate, develop new products, and do business as usual are also affected adversely. The war with Iraq, its unknown cost in a sea of rising federal deficits, and the impact on oil prices, further worsen this economic uncertainty. The most likely scenario is that this fiscal status for Missouri, and other states, will continue to play out over the foreseeable future.

In the prosperous period of the 1990s it may have appeared, to paraphrase economist Kenneth Boulding, that indeed "scarcity was dead." Our economy was reaping all of the benefits of an unprecedented set of macroeconomic conditions—substantial growth, record low inflation, and very high labor productivity. This nexus of factors transferred into record setting revenue yield for the state of Missouri. Revenues were growing so fast that it was an ongoing task to refund the annual "excess" over the constitutionally set Article X ceiling (the Hancock amendment). For FY1995-1999 almost \$1 billion was refunded to corporations and individuals due to the Hancock limit provision. At its peak in FY97, the Hancock limit was exceeded by \$319 million and required a refund [18, p. 12].

Apparently feeling that this revenue bonanza would continue indefinitely, something not characteristic of our capitalistic economy, the legislature managed to convert some of these one-time, annual refunds into permanent, on-going tax cuts even though they did not have to be made permanent. Over the course of the 1997 through 1999 legislative sessions permanent tax cuts of almost \$720 million were enacted. These cuts covered the spectrum from groceries to prescription drugs, pensions, vending machines, health insurance, and manufacturing. In addition, other de facto revenue reductions were manifest as tax credits; these amounted to \$204 million. Thus in total, just shy of \$1 billion was authorized by the legislature in tax cuts and credits. This was in addition to the Hancock refunds of \$973 million [18, p. 15].

Interestingly, during this period of unparalleled prosperity no action was implemented to move toward a systematic, comprehensive reform of the state tax structure. This had last been done in 1968, 35 years earlier [15]. Rather the policy picture that emerges from this period is "piecemeal" tax break and cuts focused on keeping below the Hancock revenue limit. This occurred in an environment of what seemed to be ever expanding state revenues. Meaningful reform in the midst of this plenty, an ideal setting, was not likely to occur.

To help set a context, it also needs to be noted that Missouri is not, and has not been, a high tax burden state. Using taxes as a percentage of personal income as a standard, Missouri has consistently ranked in the mid to high 40s. In fact for several years ranked number 50; that is, it had the lowest tax burden of the fifty states. This fiscal status led to a series in the *St. Louis Post-Dispatch* entitled "Missouri: The Forty Something State." It ran for a full week—Sunday through Friday November 25-30, 1990. At this time Missouri's tax burden was 49th. [26]

However, these fortuitous macroeconomic circumstances were not to continue. As we moved into the new millennium events impacted suddenly and hard on the state's revenue picture. These events have cumulated to date to produce the present fiscal turmoil in Missouri, as well as in most other states. Projected budget deficits are in excess of \$1 billion in Missouri and then upwards to tens-of-billions in California. Cumulatively, states confront budget shortfalls of \$30 billion to be met by July 31, 2003, and a projected \$80 billion shortfall for FY04. Without going into the details of each event, they can be identified as:

- ❖ the recession which began in 2000,
- ❖ the events of September 11, 2001,
- ❖ the burst of the *dot.com* bubble, and
- ❖ the financial turmoil produced by ENRON and its progeny.

Each of these would have taken its toll on state finances but the cumulative impact of all four together has proven to be truly profound and, arguably, far greater than the sum of the each component separately. Most scholars of state finance acknowledge that the states' fiscal status has not been "this bad" since World War II. Both the National Governors Association and the National Association of State Budget Officers, amongst many, have repeatedly echoed this sentiment over recent months.

Interestingly, Missouri state revenues are now projected to be over \$1 billion **below** the Hancock limit [5]. Some knowledgeable observers of state finance set the Hancock limit gap even greater at as much as \$1.8 billion for FY03 [20, p.4]. They also speculate that this limit, and its associated refunds, may never be an issue for the state again [20, p.5]. The effort to turn one-time Hancock refunds into permanent tax cuts worked to the tune of \$720 million but in retrospect it backfired. This \$720 million in ongoing funds would have gone a long way toward covering the deficits from earlier years and the projected deficit for FY04.

What This Study Hopes to Accomplish

The last time the Missouri state tax structure was examined in any significant detail was 1968 [15]. Important features of Missouri's tax system have not been examined in any meaningful way. They are:

- ❖ equity or fairness, that is, "who pays and how much, "

- ❖ revenue elasticity, how much automatic responsiveness to growth is built into the tax structure without the need for legislative remediation,
- ❖ efficiency, how do tax provisions affect consumer and business decisions.

Also, over this same time period, various provisions related to exemptions, deductions, credits, preferential tax treatment, etc., have propagated. These so-called "tax expenditures" have grown in scope, coverage, size, and adverse revenue impact.

In the 35 years since the last look at Missouri's tax structure, one can make a very strong case that it has changed dramatically. First, it is *old and outdated*. That is, it has not taken into account our economy's dramatic economic base-shift from manufacturing to services and from large scale firms employing thousands to small ventures with fewer than 50 employees. Also, it does not account for the dramatic growth in E-commerce and demographic shifts in the state population such as aging.

Second, as one study has so aptly labeled it, it also "leaks." [1] That is, tax expenditure provisions have drained the revenue base of dollars much like water leaking from a hole, an expanding hole, in a bucket. Services are virtually entirely exempt from the general sales tax even though consumer consumption patterns more and more favor services, knowledge-based activities, and intangibles; all of these are exempt. Tax credits and their associated cost in reduced state revenues have also grown and they are projected to reach an authorization level value of \$356 million and a redemption value of \$200 million in 2003 [7 and 20, p. 30].

This study is viewed as a first step toward examining Missouri's tax structure by attempting to attach substance and detail to Missouri's tax expenditures, its revenue "leaks." This is particularly germane in these fiscally troubled times which provide a compelling impetus to do so. It is wise tax policy at any time.

What is a Tax Expenditure?

While the definition of a tax expenditure does vary somewhat in wording given the context, the following from Oregon law captures the essence of what is meant. " 'Tax expenditure' means any law of the Federal government or this state [Oregon] that exempts, in whole or in part, certain persons, income, goods, services or property from the impact of established taxes, including but not limited to tax deductions, exclusions, subtractions, exemptions and deferrals as well as preferential rates and tax credits." (ORS 291.202–291.222).

Tax expenditures are, de facto, the equivalent of spending by the state, even though they are seldom viewed in these terms. The spending is manifest as revenue not collected due to some state law tax provision. Not collecting revenue is the same as collecting it and then returning it to the beneficiary of the special provision. It can be viewed, de facto, as a subsidy.

Tax expenditures are often, but far from always, put in place with a sound social or economic purpose, e.g., to improve equity, to encourage reduced pollution, or to promote business activity. They can be effective tools to provide incentives to accomplish social and economic objectives. However, all too frequently they are never revisited *via-á-vis* the originally articulated purpose. Often they are never looked at again *de facto* remaining a form of totally unscrutinized state spending.

While the full pecuniary impact is probably not known, it is clear that the myriad of tax expenditures cost Missouri **state** government hundreds of millions of dollars per year in foregone revenue [see **5** for detail]. Some of these provisions also cost Missouri **localities** revenue since they must adhere to state-imposed legislation, despite the cost. This local impact is quite likely to be tens of millions of dollars per year.

A revisiting of the myriad provisions of credits, deductions, exemptions, special provisions, and other tax expenditures that permeate Missouri's revenue system seem long past due. This is especially relevant in the very tight fiscal times the state now confronts and is very likely to face over the next few years. Again, it is good tax policy at any time.

A brief note on terminology is in order. *Tax expenditure* is the name associated with the myriad deduction, credit, exemption, etc., provisions of state tax law. *Tax loophole* is a phrase used to describe a tax expenditure that, for some reason, is inappropriate, egregiously overdone, or has outlived its purpose. Note however, that while use of the word "loophole," almost smacks of tax evasion, it is still tax avoidance.

Characteristics of Tax Expenditures

Tax expenditures have several characteristics that are worthy of note in the general context of state finance issues and tax policy. These characteristics clearly set them aside from the more normal budgetary process of taxing and spending.

First, they are far from "transparent." Tax expenditures are obscured or embodied in the tax structure and obvious only with some "digging" to uncover what they are. We tend to be unaware of them and their true impact. An example helps to make the point. In paying the general sales tax very few of us are aware of exactly to what the tax applies. We *may* know that food for home consumption is not taxed but are probably unaware of the status of services, motor fuel, and the myriad other "things" that are not taxed, as spelled out in Appendix 2.

Tax expenditures are not well understood or recognized by the average taxpayer. This may be true in a legislative context as well in that the full implications for state revenue are not spelled out. Beyond the revenue

implications, per se, there are the incentives that tax expenditures give due to the de facto subsidies that they provide to certain types of activity or inactivity.

Second, tax expenditures generally are "open-ended." One can take advantage of these provisions to the maximum since there is no limit on how much you may benefit. As an example, prior to the passage of Senate Bill 380 in 1993, Missourians could deduct all federal income taxes against their Missouri taxable income, no matter how much. Quite simply, the more you paid, the more you could deduct. While this is no longer true (it is capped at 50 percent), it was up until 1993. These deductions were limited under SB380 to raise funds for school finance reform. Elimination of this open-ended provision yielded upwards of \$300 million for school funding. To the contrary, Social Security taxes remain fully deductible in determining Missouri taxable income. Missouri is one of only three states that has such a provision at an estimated cost in state revenue of \$235 million for 2003 [5, p. 9]. In addition to being open-ended, there is most often no "sunset" provision to eliminate or phase out the tax expenditure and its associated state revenue loss.

Third, tax expenditures are seldom, if ever, subject to legislative or executive scrutiny. They are a part of the tax system that generally goes without review; they have often been referred to as part of the "hidden" budget. This is curious since they are, de facto, a type of spending by state government. They are spending, or if you like a subsidy, in the sense that if you qualify the deduction reduces your tax liability. Allowing you not to pay taxes is the same thing as giving you an equivalent amount of money. This cost the state reduced tax yield. While the normal budgetary process subjects spending to rigorous and very detailed scrutiny and review, such is not the case with scores of tax expenditures that cost Missouri hundreds of millions of dollars in lost revenue [see 5, p.2].

In most respects tax expenditures are "outside" of the normal budgetary process. And yet, they have a profound impact on state finances. The lost tax yield that they represent clearly is one dimension to the fiscal turmoil that many states now confront. Revenue shortfalls can be linked to the revenue reductions associated with specific tax expenditure provisions. The tax base for the state's two major revenue generators, general sales, and individual income, has been eroded through these provisions. In addition and perhaps even more damning for the general sales tax, the definition or scope of its base has been narrowed to tangible items that are a shrinking proportion of consumer spending. This shrinking base can only keep up as a revenue generator through economic growth or rate increases.

Presently, 37 states publish tax expenditure reports but they vary considerable in quality and coverage. Missouri is one state that publishes a report of high quality [5]. As the fiscal situation worsens, states will (and have already) look much more closely at tax expenditure "loopholes" as a means of enhancing a stressed revenue base. Their lack of transparency, open-ended nature, and isolation from executive and legislative review will be challenged.

Establishing a Set of Criteria

In order to review the tax expenditure situation in Missouri a set of criteria was proposed for consideration to allow those provisions most subject to challenge and question to be isolated. They can then be considered as part of a revenue enhancement package. The intent is not to throw open all tax expenditures, many serve a valuable social or economic purpose, but to allow those that do not to be scrutinized. Also, it should not be inferred that tax expenditure elimination is the answer to Missouri's present overall budget situation. It can make a contribution.

The following reflects a set of criterion that might reasonably be employed for such a purpose. They have been developed drawing on a variety of sources including: a review of the literature on tax expenditures; Department of Revenue staff; Office of Administration, Division of Budget and Planning staff; input from public meetings; input from meetings and feedback from business and other groups; and the Department of Revenue's Director's Advisory Group. While this list is not exhaustive it is reflective of major concerns about tax expenditures and their fiscal impact on Missouri.

One expectation at the outset of this study was that the information required to subject each tax expenditure to the following set of criteria either would not be available or would be available at a very high cost in time, money, and other resources. This, in fact, proved very much to be the case. With the exception of the tax credits administered by the Department of Economic Development (DED), the data and information on their impact are dismally small. DED does provide much analysis in the form of the impact of the credits they administer, more on this later in the report.

The legislation, generally, is not written with this built-in requirement for evaluation of a tax expenditure provision in mind. The focus is narrow with evaluation either before or after the fact not an expected outcome. Missouri's *Tax Expenditure Report* has been prepared 11 times pursuant to RSMo 33.283 since 1989 and provides a very high-quality and detailed "catalog" of Missouri state tax expenditures [see 5 p. ii]. Its mandate, however, is to catalog not to evaluate.

A useful model to perhaps be applied in Missouri is the one developed by the state of Oregon. Their report examines 293 tax expenditures within 15 Oregon tax programs. The legislative act, requiring this analysis, the 1995 Budgetary Accountability Act, specifies that the following items be considered:

- ❖ statutory authority,
- ❖ purpose enacted,
- ❖ current revenue loss,
- ❖ previous revenue loss,
- ❖ is it the most effective way to achieve the purpose,
- ❖ has it achieved its purpose,

- ❖ who benefits from the provision,
- ❖ is it sunset,
- ❖ if sunset, should the sunset take effect or be revised, and
- ❖ what program or function does it support.

Enacted in 1995, the first report was prepared for the 1996-97 biennium. The latest is for 1999-2001. Oregon notes the constraints of incomplete information and limited resources but also substantial progress toward providing complete information.

With the criterion set out in this Oregon work as background, we can shift attention to Missouri. The full set of criteria that have been set out for consideration in this study are given below. They have been derived from the groups mentioned earlier.

- ✓ how many are there,
- ✓ how have they increased in number,
- ✓ length of time in place,
- ✓ original or modified purpose,
- ✓ continued relevance of stated purpose,
- ✓ present cost of provision,
- ✓ growth of cost in the past and projected into the future,
- ✓ what has been accomplished, did it serve the original purpose,
- ✓ the distributional impact, in any,
- ✓ is there a sunset provision,
- ✓ efficiency, can it be done at a lower cost,
- ✓ administrative ease and cost,
- ✓ compliance costs,
- ✓ does it add to the complexity of the tax system,
- ✓ transparency -- how much is "hidden" from legislative or executive scrutiny, and
- ✓ what are the unintended consequences, such as local revenue implications, If any.

The analysis does not account for the following:

- ✓ the behavioral changes if the tax expenditure was to be eliminated,
- ✓ the fact that a beneficiary may qualify in more than one place,
- ✓ that administrative constraints may preclude collection of full liability, and
- ✓ that they may interact and thus the full cost is not simply the sum of individual tax expenditures.

Findings

This section will be broken into two components. First will be an overview discussion of Missouri's tax expenditures. This will attempt to spell out what is in place. Second, more specific attention will be given to tax credits since they receive much more scrutiny and evaluation than other tax expenditures.

Generally, it was found that the level of detail required to subject Missouri's tax expenditures to the set of criterion given above is not readily available or does not exist. Whether or not they meet certain criteria can be answered in some instances but major questions related to their intended purpose, achieving this purpose, and their efficiency, administrative and compliance ease and cost, and unintended consequences all remain in need of much more analysis. The cost of this analysis in terms of time and resources will not be trivial.

Summary of Missouri's Tax Expenditures

Missouri has a wide range of tax expenditure provisions. As mentioned earlier they are fully catalogued in the statutorily mandated study *Tax Expenditure Report* [5, for various years] which has been done eleven times since the legislation was first passed in 1989. Missouri's tax expenditures, de facto, apply to each of the following types of taxation, but to varying degrees:

- individual income
- corporation income
- sales and use
- corporation franchise
- insurance premium
- specific excise

In sheer number however, most of them affect the corporation, individual income, and sales and use tax. Missouri's *tax credits* can be applied against any of the above taxes except the specific excise taxes.

Appendix 1 outlines items that reduce the tax liability for Missouri taxes that are affected by tax expenditures; it includes tax credits. Appendix 2 does the same but for sales and use tax. Appendix 3 provides detail from DED on their tax credits for FY1999-2004 by type and by their status, i.e., authorized, issued, and redeemed. Table 1 summarizes tax expenditures that affect Missouri taxes by type of tax. Several comments are in order so that this information is properly interpreted.

First, the Missouri individual and corporation income taxes reflect myriad provisions of federal tax law. These laws incorporate numerous provisions for what are, de facto, tax expenditures. Since Missouri has adopted the federal definitions for income, statutory adjustments, and itemized deductions, they are intertwined with state tax law and these tax preferences get "passed though" to become state tax expenditures. These are *in addition to* Missouri specific provisions such as those that affect pensions, itemization of social security and railroad retirement taxes, and tax credits.

Second, the sales and use tax does not apply to a multitude of services under Missouri law such as medical, legal, repair, and professional. Under a comprehensive definition of what is entailed by retail sales, these items would be included, similar to the VAT tax used in Europe. However, these services have

never been taxed in Missouri since the sales tax was enacted in 1934 (the use tax was enacted in 1959).

TABLE 1
A SUMMARY OF MISSOURI'S TAX EXPENDITURES
BY TYPE AND BY TYPE OF TAX

<u>Tax Item</u>	<u>Number of Tax Expenditures</u>
<i>Individual Income Tax:</i>	
Federal and Missouri exclusions from gross income	95
Missouri adjustments	6
Missouri deductions from adjusted gross income	24
Missouri credits	52
<i>Corporation Income Tax:</i>	
Federal exclusions and deductions from gross income	46
Missouri exclusion	1
Missouri deductions	4
Missouri credits	48
<i>Sales and Use Tax:</i>	
Missouri exclusions from gross receipts	16
Specific exemptions (see Appendix 2 for full detail)	115
Credits	1
<i>Corporation Franchise Tax</i>	
Missouri exclusions and deductions	1
Missouri credits	26
<i>Insurance Premium Taxes</i>	
Missouri deductions	3
Missouri credits	38
<i>Selected Excise Taxes:</i>	
Liquor and beer	none
Cigarette	1
Tobacco	none
Motor fuel	1
<i>Inheritance and Estate Taxes:</i>	<i>none</i>

Source: Appendices from [5] for year 2002.

The issue here is one of fundamental importance to state finances in Missouri and all other states that tax retail sales. Services some 70 years ago in Missouri were of very little importance in consumers' expenditure patterns. This is not the case in 2003. Services dominate consumer expenditures and will do so even more in the future. This means that the present sales tax base is a shrinking portion of consumer expenditures. This also means that there is constant pressure for this tax to keep up with revenue requirements. What in the past had been a revenue mainstay for state finance is diminishing in importance due to the relative shrinkage of its tax base.

Third, the number of specific exemptions listed under the sales and use tax actually are far more numerous in full detail. Appendix 2 spells out 115 specific sales and use tax exemptions; the text emphasis in ***bold italics*** indicates the item(s) affected. Finally, the tax credits listed in Table 1 with each type of tax are not necessarily unique to that tax. The same Missouri tax credit can be taken against more than one tax and more than one credit can be taken against a single tax. Thus, these numbers should not be added together.

Non-Tax Credit Tax Expenditures

Appendices 1 and 2 show Missouri's non-tax credit tax expenditures. Matching them up with the criterion set out above has proven to be a daunting task. This is in many respects far beyond the scope of this analysis and remains open for future study, as will be discussed below. Some comments are, however, in order. First, the best information available for these tax expenditures is their dollar impact on state coffers. This has been reported since 1989 in the *Tax Expenditure Report [5]* which has been recognized in other states as a model for replication. This piece of the puzzle seems well in place.

Most of the other criterion can be lumped together, at present, as simply not being addressed at all, with an occasional exception. They are:

- ❖ capping of the fiscal impact,
- ❖ legislative or executive review or scrutiny,
- ❖ transparency,
- ❖ distributional impact,
- ❖ unintended consequences,
- ❖ efficiency,
- ❖ sunset provision, and
- ❖ administrative and compliance ease and cost.

This is not to say these issues could not be addressed but generally that they are not at present. Extensive further study and analysis would be required. As noted below this is a worthy endeavor for state tax policy.

As to purpose and relevance of purpose the issue is somewhat clearer but still remains mostly hidden in the legalese of statutory language. Appendix 2 indicates in ***bold italics*** what each provision seems to apply to. This is not the same as its "purpose" in a more meaningful sense but it is a first step. Much more work needs to be done.

Tax Credits

As of December 2002 there were 51 tax credit programs in Missouri. Most of them (33) are administered through the Missouri Department of Economic Development (DED) [7, p.2]. Note that the number of DED tax credits does not match for all sources due to the use of different years. Appendix 3 shows detail by year, type, and status. The largest of those not under DED relate to the senior citizen property tax, insurance, and pharmacy but also includes, but is not limited to, shared care, disabled access, maternity home, and special needs adoption [5].

The tax credits administered by DED generally apply to some facet of economic development for the state of Missouri and can be applied against one or more of the following state taxes:

- corporation income
- individual income
- financial institution
- corporate franchise
- insurance premium
- fiduciary

The tax credits fall into one of the following six program categories shown in Table 2:

Unlike other Missouri tax expenditures, DED has done considerable work to expose the tax credits under its purview to scrutiny and review. Some statutes require that a cost-benefit analysis be done. However, DED lacks the required statutory authority to require information that may reflect the success or failure of its 15 non-discretionary programs [7]. The Missouri's State Auditor's Office has discussed this in two recent reviews of DED tax credits. As noted in its reports there are still problem areas [16 and 17] such as:

- the state does not track outstanding tax credits,
- the economic impact of credits is hard to determine due to poor, project-level data,
- overestimating credit redemption skews the state budget through faulty revenue projections, and
- better project benchmarks are needed.

"State law mandates the State Auditor's Office perform cost-benefit analyses on the 35 tax credit programs administered by the Department of Economic Development." [17, p. 1] Of the 35 tax credits listed in the Auditor's report of 2002, only ten had been reviewed [17, p. 54]. DED has taken significant steps to monitor and evaluate its tax credit programs.

TABLE 2
A SUMMARY OF MISSOURI TAX CREDITS
ADMINISTERED THROUGH DED

Program	Non Discretionary	Total Number	Number Capped	FY02 Redeemed Credits (\$ millions)
Community development	2	5	5	\$15
Redevelopment	2	5	3	61
Business recruitment	3	7	4	26
Training	2	3	3	11
Housing	1	3	3	26
Entrepreneurial	<u>5</u>	<u>8</u>	<u>6</u>	<u>23</u>
Total	15	31	24	\$161

Source: [7].

A recent study of the current Missouri budget problem looked at tax credits and concluded that they need to be curtailed, be more closely reviewed, and that the "tail" of credits needs to be more fully understood in terms of its impact on the state revenue picture [20, p. 32]. This "tail" refers to credits that have been both authorized and issued but not yet redeemed. When actually redeemed they reduce state revenues.

This same author, in an earlier report, commented on a study prepared for the Missouri Development Finance Board in March of 2000 for 18 tax credit programs administered through DED. He noted that there was a positive \$2.24 billion present value impact on state revenues due to these programs [18, p17-19]. This strongly suggests that they are accomplishing their purpose but that monitoring, review, and evaluation are still required. Also, the programs might be condensed or coordinated to be more effective. DED seems to be doing just this [7, pp. 19-22]. The close scrutiny of tax credits at this point in time is a direct function of the state's deteriorating budget situation and a questioning of what it can "afford." It is also wise tax policy.

In summary, Missouri tax credits administered through DED do provide information related to the criteria set out above. Their purpose is clearly identified as enacted or modified; their cost is tracked over time with the exception of the credit "tail"; they are subject to scrutiny albeit not necessarily each year during the budget cycle; they are transparent; ex post evaluation is done; and questions are raised about "doing things" more efficiently. Proper evaluation would allow the extent to which they meet their intended purpose to be addressed. Unintended consequences, while not mentioned explicitly, should fall under the rubric of a thorough program evaluation. Also, there is no mention made of

"sunsetting" but it has been discussed in the context of DED's *2003 Economic Agenda--Tax Credits* [7, pp.19-22].

DED has already undertaken the process of eliminating, refocusing, sunsetting, and targeting its tax credits in light of state budget shortfalls. As a form of tax expenditures for Missouri, DED tax credits receive a considerable amount of attention vis-à-vis the suggested criteria. However, this information would be much more useful if it was organized and available in a single format for review.

Information on other tax credits is much more difficult to come by. Their cost is tracked in part in the *Tax Expenditure Report* [5]. Their purpose seems to be most closely linked to the income status of Missourians who qualify, either residents or their housing. One problem with lack of evaluation of such programs emerged in early 2001 with the Pharmaceutical Tax Credit Program. It was estimated to cost \$20 million but came in at almost \$90 million thus contributing significantly to the 2001 state revenue shortfall. As a result, it has since been converted into a regular budget expenditure item for low income seniors [20, p.29 and 17, p.3].

Budgetary Implications

A search through Missouri's myriad tax expenditures proved frustrating in terms of matching with the criterion set out earlier. However, certain items did stand out as potential candidates for reform or elimination. They fall much closer to the label of tax "loophole" than tax expenditure. Appendices 4 and 5 contain detail on these items. Appendix 4 has items for which more information has been developed. Appendix 5 contains items for which more study is needed. These are not all of the items that might qualify for modification or actual elimination but they represent a good start. They will not solve Missouri's budget dilemma, no single item will. They would contribute to softening it and should be considered in executive and legislative deliberations.

Tax credits administered by DED also need to be examined for revision, restructuring, or elimination. As noted in a recent report they have been growing in dollar cost to the state and the "tail of outstanding tax credits has increased the uncertainty surrounding state revenue estimates [20]. The author of this report suggests a 40 to 50 percent reduction [20, p.32] and it seems wise to build on what DED has already begun [7]. Again, tax credits by themselves will not solve the state's budget situation but it is yet another piece in a very complex state fiscal puzzle.

In Closing --Toward a Tax Expenditure Policy Agenda for Missouri

This study has attempted to examine tax expenditures in the context of Missouri's state finances. These provisions have an impact on the revenues available to the state. They also have an impact in terms of the purpose for which they were intended be it social, economic, or something else. It was found that excellent data are available on the cost of most tax expenditure provisions over time but that evaluation virtually stops there.

A next logical step for the state would be to set in motion a process to allow regular and full evaluation of all of the state's tax expenditures. DED has made considerable progress on the tax credit portion of such an analysis and much could be garnered from their work. More needs to be done, however. Other tax expenditures remain virtually without evaluation with the exception of the excellent attempts to quantify their dollar impact in the *Tax Expenditure Report* [5].

This process would need to include a selection of what is to be examined, a determination of a final set of criterion for evaluation, program identification with tax expenditures where appropriate, and coordination of those state agencies that have the information and expertise to do the analysis. An excellent guide for this is provided by the state of Oregon which began just such a process in 1995 for their nearly 300 tax expenditures [23]. The first report covered the period FY1996-97 and the second FY1999-2000. They have noted that the process is slow and has been limited by information but also that considerable progress has been made. Missouri could do the same. It is good tax policy. Table 3 provides a template of the Oregon model which could be expanded and adapted to Missouri.

TABLE 3	
A TEMPLATE FOR TAX EXPENDITURE EVALUATION	
Program Category–Tax Type	
Statute(s):	
Sunset Date:	
Year Enacted:	
Earlier Year(s) Revenue Impact	dollar amount
Current Year Revenue Impact	dollar amount
Description:	
Purpose:	
Who Benefits:	
In Lieu:	
Evaluation:	
Source: [23].	

It is suggested that Missouri begin the process of more detailed evaluation of its myriad tax expenditures. Only then will a full understanding of their cost, intended purpose, and achievements be available. Only in this context can they be linked in a meaningful way to the normal, annual budgetary process.

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