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Nixon-Kraus Tax "Deal" Would Undercut Missouri Services, Including Education

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Governor Nixon announced this week that he has reached a preliminary agreement with Senator Will Kraus on tax cuts. The proposal, as announced, is skewed to benefit Missouri's wealthiest families and leaves all services vulnerable to cuts as a result of the deal's $364 - $500 million cost.

Framework of Governor Nixon/Senator Kraus Deal

Governor Nixon indicated that he may be willing to support a tax cut in Missouri, if it contains the following components:

- A reduction in the top individual income tax rate of .25 percent (lowering the rate from 6 percent to 5.75 percent), contingent on $200 million in revenue growth and fully funding the K-12 foundation formula;
- A further .25 percent reduction in the top rate (lowering the rate from 5.75 percent to 5.5 percent) if the low income housing tax credit program is capped at $110 million and the historic preservation tax credit is capped at $90 million.

While official bill language has not yet been released, analysis of the impact of lowering the top individual income tax rate *and* assessing the general framework of his proposal indicates more harm than good for Missouri families.

Most Missourians Would Receive Little Benefit

A reduction in the top individual income tax rate is skewed to most benefit very wealthy families rather than average Missourians. In fact, analysis by the Institute on Taxation and Economic Policy shows that under this proposal, 76 percent of the tax reduction would fall to the wealthiest 20 percent of Missourians. **The highest income Missourians – those with average incomes over $1.094 million – would receive a tax cut averaging $3,779 per year. In contrast, the average Missouri family with incomes from $33,000 - $52,000 would receive just a $47 tax cut per year**, about enough to buy one hamburger each month. And the lowest income Missourians, those with incomes under $18,000, would get zero benefit.

All Missourians Negatively Impacted by Reductions in Services

While bill language is not yet available, a review of the proposal's components indicates that cuts to education, public safety, infrastructure, or other services would be required. At minimum, the proposal would reduce state income tax revenues by $364-$500 million per year when fully implemented[1]. In context, the amount is the equivalent of the current shortfall in Missouri's K-12 school funding formula.

[1] Based on analyses conducted by the Institute on Taxation & Economic Policy and the Missouri Budget Project (MBP); Missouri Budget Project analysis based on FY 2014 individual income tax collections estimated at $5.39 billion. The estimate is found in the Missouri Senate Appropriations Committee, "2013 Annual Fiscal Report" available at: www.senate.mo.gov

As outlined, the proposal would make the second drop in the top income tax rate contingent upon placing caps on existing tax credits. Specifically, the Historic Preservation credit would be capped at $90 million, and the Low Income Housing Tax Credit would be capped at $110 million, for a combined $200 million cap. In fiscal year 2013, Missouri spent $223 million on these two credits.[2] In theory, the new caps could result in about $23 million in savings, which could then be used to slightly offset the tax reductions. However, the savings would not be nearly enough to pay for the full amount of the tax cuts. While the proposal would require that general revenue grow by $200 million compared to the average of the last three fiscal years prior to the tax cuts being implemented, that amount is not even sufficient to make up for inflationary needs. Further, there is nothing indicated that would require revenue to continue to grow *after* the tax cuts are implemented. In other words, there is no scenario in which the proposal does not reduce revenue available for state services.

K-12 Education Funding May Also Be Vulnerable

The Governor's office announced that the proposal would contain a provision to ensure that the K-12 funding formula is fully funded before the tax cuts are implemented. **However, there are no ongoing protections for funding of public education.** Once the tax cuts are implemented, funding for local schools could again be reduced. Further, there is nothing in the proposal outline that would protect the array of services that support access to quality education including funding for school transportation, the Parents as Teachers and First Steps early intervention programs, and other educational services.

In addition, even if lawmakers did choose to protect K-12 funding in an ongoing manner, the burden of the required cuts brought about by reductions in state revenue would simply be pushed to other critical public services. These services include investments in quality preschool through higher education that provide Missourians with opportunity for success, mental health, health & child welfare that help Missouri families who are most in need, investments in public safety for our communities, and investments in our infrastructure for a strong economy.

There is A Better Way

The legislature is currently considering alternative tax change proposals. **Some of these proposals would be much more effective at helping average Missouri families in a fiscally responsible way.** For example, the House Ways and Means committee recently approved a substitute for House Bill 1120. The bill would create a state earned income tax credit (EITC) equal to 10 percent of the federal earned income tax credit (EITC). The federal earned income tax credit has proven to be effective in reducing poverty, encouraging work and even increasing the educational attainment of children in fixed income families.[3] Because of the success of the federal EITC, twenty-six states have established their own state EITCs, including several of Missouri's neighbors: Oklahoma, Kansas, Iowa, and Illinois.[4]

In the 2013 tax year, working families with children that have annual incomes below about $37,900 to $51,600 (depending on marital status and the number of dependent children) may be eligible for the federal EITC. Also, working individuals that have incomes below about $14,300 ($19,700 for a married couple) can receive a very small EITC.[5] **In tax year 2011, the most recent year for which the data are available, 514,367 Missouri families received the federal EITC.[6]** In that year, the average federal EITC was $2,905 for a family with children, boosting take home pay by about $240 a month.[7]

Perhaps most important, the substitute for HB 1120 would cost just over $100 million per year. That amount is more fiscally sustainable for Missouri, allowing the state to provide a tax reduction that would help average Missourians while simultaneously protecting funding for services.

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[2] Missouri Senate Appropriations Committee, "2013 Annual Fiscal Report"
[3] For more information, see "Earned Income Tax Credit: A Targeted Tax Change with Significant Impact," Missouri Budget Project
[4] Center on Budget & Policy Priorities, "Policy Basics: State Earned Income Tax Credits," January 2014
[5] Ibid
[6] Brookings Institute EITC interactive, data from tax year 2011
[7] Center on Budget & Policy Priorities, "Policy Basics: The Earned Income Tax Credit," January 2014