

Frequently Asked Questions about Missouri's Income Tax Revision Proposal

Question: What does this bill accomplish?

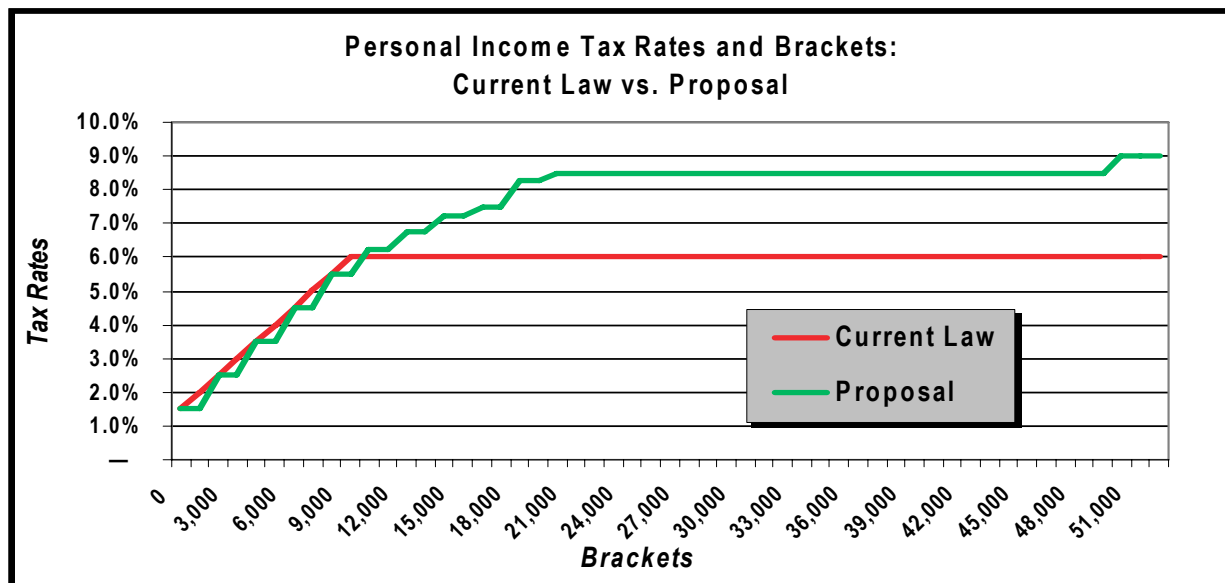
Answer: This legislation changes Missouri's individual income tax rates and tax brackets, repeals Missouri's income tax deduction for federal income taxes paid, and provides tax relief for low-income taxpayers by introducing a new low-income credit. This bill is estimated to increase Missouri revenues by \$1.3 billion, while cutting taxes, on average, for the poorest 60% of Missourians.

Q: What's wrong with the current income tax brackets?

A: The following are Missouri's current individual income tax brackets. The rates and brackets apply to taxable income, not total income and are used to compute tax liability after all deductions, adjustments, and exemptions are calculated. For example, a single person with no children who earned \$25,000 in 2007 has taxable income of \$16,250 after claiming the personal exemption and standard deduction.

The top bracket hasn't been changed since 1931. Because the current tax brackets are so narrow, nearly sixty percent of Missourians are now paying at the top income tax rate. The red line on the chart below illustrates Missouri's current individual income tax rates and brackets.

Q: What are the new income tax brackets in this proposal?



A: This proposal reforms the current individual income tax brackets and introduces more progressive and graduated rates and brackets. These wider tax brackets range from 1.5 percent to 9 percent and ensure that low and middle income taxpayers pay at lower tax rates, than do the very wealthiest Missourians.

Q: What is the deduction for federal income taxes paid?

A: Missouri is one of only seven states that allows a deduction for federal income taxes paid. Current law allows Missourians to subtract up to \$5,000 of federal income tax liability (\$10,000

for married filers). This is a costly and poorly targeted deduction that offers no benefit to the many low and middle income Missourians who don't owe federal income taxes.

Q: How does this proposal change the deduction for federal income taxes paid?

A: This proposal eliminates the deduction completely. The deduction is most beneficial for wealthier taxpayers who have a higher "ability to pay." For the wealthiest 40 percent this will mean their taxes will increase, but these same taxpayers will see some offsetting benefit from the "federal offset" (see next question).

Q: What is the Federal Offset?

A: Federal income tax rules allow taxpayers to claim itemized deductions for certain expenditures that affect their ability to pay taxes. For example, you can use these deductions to offset part of the cost of charitable contributions, mortgage interest payments for homeowners, and state and local income and property tax payments. These deductions make it less costly to pay state or local taxes. The ability to deduct or "write off" these taxes on your federal tax forms means that if you itemize your federal taxes, some of your state taxes are being directly offset by federal tax cuts.

The practical impact of being able to write off these state and local taxes is that if you itemize your federal income taxes, your state income tax and property tax bills are never really as big as they appear. Some portion of the state taxes you pay initially will be directly offset by federal income tax cuts when you file your federal tax forms.

Q: How does this proposal take advantage of the federal offset?

A: This bill does a very good job of taking advantage of the federal offset. The tax increase imposed by this individual income tax reform is targeted to the wealthiest 40 percent of Missourians. These wealthy Missourians are also more likely to itemize and pay tax at higher federal rates, which means they can write off a larger percentage of their state tax hike. In fact, 20 percent of the added state revenue from this tax hike would be paid for not by Missourians, but by the federal government.

Q: How would the new low income credit work?

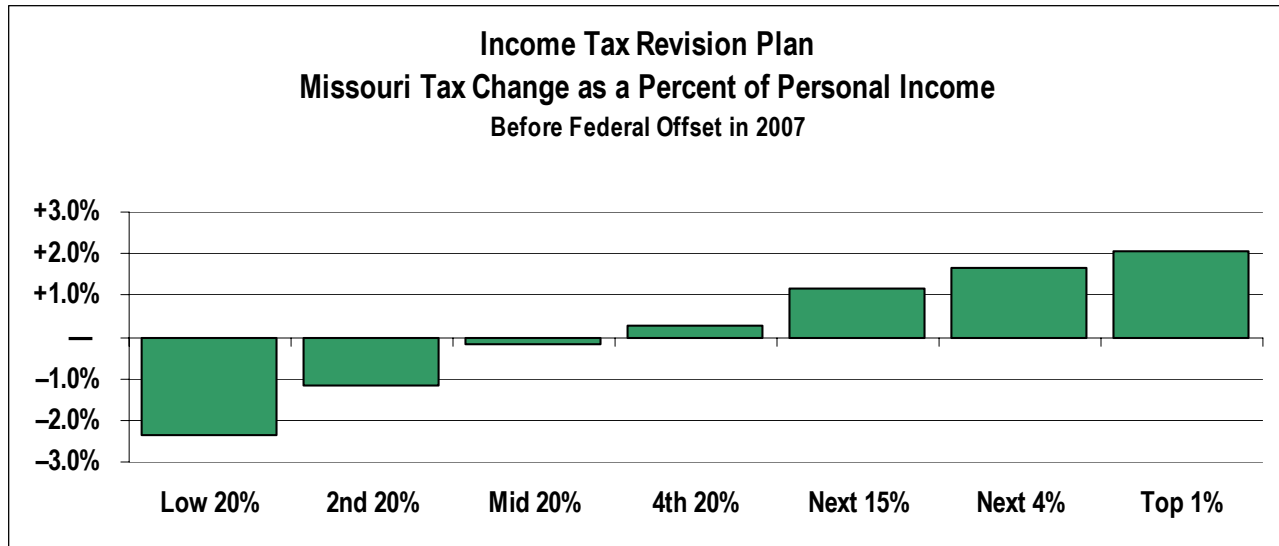
A: The new low-income credit provides targeted tax relief for those Missourians who are most in need. The proposal provides a tax credit of \$150 per family member. (In other words, an eligible single taxpayer would receive a \$150 tax credit, while an eligible family of four would receive \$600.) The credit is phased out over a straight line for higher-income taxpayers between \$30,000 and \$50,000 (\$60,000 and \$80,000 for married couples) of Federal Adjusted Gross Income. Perhaps most important for low income Missourians, the credit is refundable which means that low income Missourians can use the credit to offset the other regressive taxes they pay.

Q: How much money does this proposal raise?

A: This bill increases state revenues by over \$1.3 billion. Federal taxes for itemizers are reduced by \$264 million (through the federal offset) for a net tax increase on the wealthiest Missourians of just over \$1.0 billion.

Q: What is the average tax change for Missourians under this proposal?

A: The following graph illustrates the percent of tax change by income level under this proposal.



- The poorest twenty percent of Missourians, those with an average income of \$9,000, experience an average tax cut of about \$224.
- The next twenty percent of Missourians, those with an average income of \$22,000 experience an average tax cut of \$249.
- The middle twenty percent, those with an average income of \$37,000 experience an average tax cut of \$55.
- The fourth 20% of Missourians, those with an average income of \$59,000 would experience an average tax hike of \$152.
- The next 15% of Missourians, those with an average income of \$98,000 would experience an average tax hike of \$1,161.
- The next 4 % of Missourians, those with an average income of \$213,000 would experience an average tax hike of \$3,491.
- The wealthiest 1% of Missourians, those with an average income of \$1,116,000 would experience an average tax hike of \$23,100.

Q: What aspects of Missouri's current income tax are left unchanged under this proposal?

A: Much of Missouri's income tax structure will remain unchanged after the passage of this legislation. The standard deduction, personal exemption, pension exclusion, and aspects of Missouri's tax structure that are linked to the federal will remain unchanged under this proposal.