Legislative Analysis

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INCOME TAX RATE REDUCTIONS

House Bill 5265
Sponsor: Rep. Pat Somerville

House Bill 5266
Sponsor: Rep. Tim Kelly

House Bill 5267 (Proposed H-1)
Sponsor: Rep. Jeff Farrington

Committee: Tax Policy
Complete to 2-11-14

A SUMMARY OF HOUSE BILLS 5265 AND 5266 AS INTRODUCED 1-29-14 AND HOUSE BILL 5267 (PROPOSED SUBSTITUTE H-1)

<u>House Bill 5267</u> would amend the Income Tax Act to do the following:

- Lower the income tax rate from the current 4.25% to 4.15% on and after October 1, 2014.

- Reduce the rate on and after January 1, 2016, to 4.05%.

- Beginning October 1, 2017, and each October 1 thereafter, lower the rate by 0.1 <u>if</u> total General Fund/General Purpose revenue in the immediately preceding fiscal year increased by $300 million or more, and that increase was at least the rate of inflation for that year. (This means the first available such reduction would take the income tax rate to 3.95%.) However, the rate could not be reduced for two consecutive years.

- The determination that General Fund revenue has increased as required would be made by the state treasurer based on an official economic forecast determined at a revenue estimating conference. [As written, the bill appears to base the determination of sufficient increased revenues on a *forecast* rather than on the *realization* of revenues.]

<u>House Bill 5266</u> would:

- Lower the income tax rate from the current 4.25% to 4.15% on and after October 1, 2014, and before January 1, 2016.

- Reduce the rate on and after January 1, 2016 to 4.05%

<u>House Bill 5265</u> would lower the income tax rate from the current 4.25% to 4.15% on and after October 1, 2014.

The bills are not tie-barred to one another, meaning any one of the bills could be enacted and take effect without the enactment of any of the others. [Note that if all three were enacted, they would need to be signed in numerical order.]

FISCAL IMPACT:

The two individual rate cuts are expected to reduce net income tax revenue by $222.0 million in FY 2014-15, $405.7 million in FY 2015-16, and $419.3 million in FY 2016-17. The combined impact of the two rate cuts (relative to current law) will continue to increase in subsequent years.

Given that the trigger depends on the future growth of GF/GP revenue, it is more difficult to ascertain a fiscal impact beyond FY 2016-17. However, even if an average annual growth rate of less than 3% is assumed for GF/GP revenue, the triggered rate reductions could potentially occur every other year. Because the trigger remains constant and is not adjusted for inflation, it becomes a smaller percentage of overall GF/GP revenue, which increases the likelihood of more frequent rate reductions. Net GF/GP revenue estimates from the January 2014 Consensus Revenue Estimating Conference projected a 5.0% increase in FY 2014-15, a 4.9% increase in FY 2015-16, and 3.6% increases in both FY 2016-17 and FY 2017-18.

The revenue impact of each rate reduction would become increasingly larger under the assumption that the income tax base grows, and within a 10-years period a single 0.1% decline in the rate could reduce income tax revenue by as much as $350 million in a fiscal year.

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