BRIEF

TAX REFORM

Louisiana Budget Project

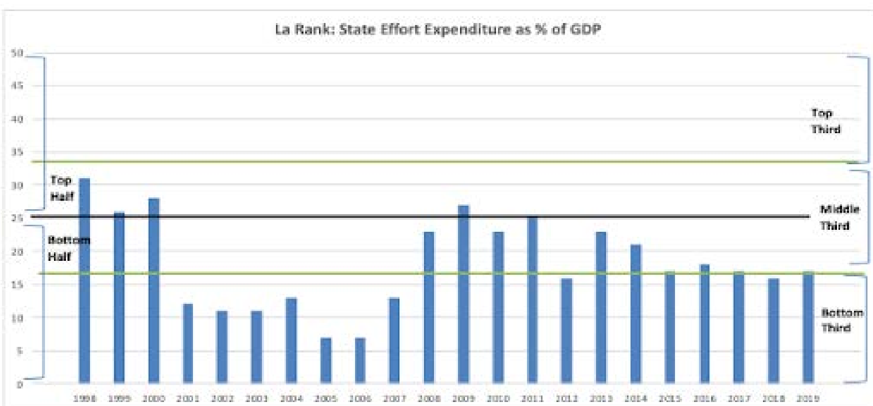
A Path Forward for Louisiana Tax Policy

For Louisiana to reach its full potential, all of its citizens need access to high-performing schools, safe communities, good roads and public transportation, affordable health care, and a safety net in case they fall on hard times. Paying for these public services requires a tax structure that raises adequate revenue in ways that are both fair and sustainable.

Any discussion of tax policy should start with two fundamental questions: How much revenue do we need to raise? And who should we raise that revenue from? Unfortunately, Louisiana's current tax structure falls short on adequacy, sustainability and fairness.

Louisiana's current revenue structure is inadequate. When measured against the overall state economy, Louisiana's state government footprint is smaller than most - typically in the bottom one-third. We see the results of this under-investment in the state budget. Even in the current year - when revenues are strong by historical measures - there are significant unmet needs across the state.

How Large Is Louisiana State Government Compared to Other States?



Source: Legislative Fiscal Office

- Our teachers are paid several thousand dollars below the Southern and national average, which is making it harder for school districts to ensure that every classroom has a strong, highly qualified teacher.
- Our child welfare system is broken and unable to care for Louisiana's most vulnerable children, in part because state investments in this critical service are down 30% since 2008.
- Louisiana's early care and education system is being supported by $200 million in temporary federal funding that needs to be replaced next year with state funding, or else 16,000 young children will lose their access to the high-quality child care services they are currently receiving.

Louisiana's tax structure is also unfair, in that people at the bottom of the income ladder pay a higher percentage of their income in state and local taxes than those at the very top. The Institute on Taxation and Economic Policy - ITEP - calculates that households in the lowest 20 percent of income, making less than $17,100 per year, pay nearly 12% of their income in state and local taxes, while those in the top 1% pay a little over 6% of their income in taxes. This, of course, is because of the type of taxes we charge at the state and local level. Louisiana has the highest combined sales tax rate in the country, while our per-capita income tax collections are near the bottom (No. 37 in the country, according to the Tax Foundation - and only 41 states have a personal income tax).

Our tax structure is unstable. If this Legislature does nothing, Louisiana's general fund revenues will shrink by at least $800 million a year by 2025. This is because of tax policy that's already on the books: A temporary .45-cent sales tax that expires at the end of the 2025 fiscal year, and the decision to shift vehicle sales taxes from the state general fund to a transportation trust fund. This $800 million is revenue that supports public schools and college campuses, hospitals and nursing homes, and all the other services that Louisianans depend on.

MOVING FORWARD

There are several steps the state can take to make our tax structure more fair, adequate and sustainable. The goal should be to avoid the upcoming fiscal cliff by replacing the revenue that will be lost due to tax cuts and revenue shifts, and to ensure Louisiana has enough revenue available on an ongoing basis to fund the education, health, infrastructure and safety-net needs of its citizens:

Tax credits

- Double the state Earned Income Tax Credit (EITC) from 5% to 10% of the federal credit. Louisiana was the first state in the South to enact a state EITC, but our credit is currently tied for the second-lowest among the more than two dozen states that have an EITC.

- Cap or eliminate tax credits that are ineffective. The Quality Jobs program costs more than $150 million a year, but the Legislative Auditor estimates that it brings in, at best, 10 cents of state tax revenue for every $1 paid to eligible corporations. The $180 million per year Motion Picture Investor and Infrastructure Tax Credit produces similarly low returns on investment.

Individual Income Tax

- Raise the top income tax rate to 4.75% from the current 4.25%. Income taxes are the most progressive part of Louisiana's tax structure, in that the highest rates apply to those with the highest incomes. A top rate of 4.75% would still leave Louisiana below neighboring Arkansas and Mississippi, and tied with Oklahoma.

- Eliminate trigger language. The 2021 tax revamp that lowered the income-tax rates on individuals and corporations included a provision that calls for automatic, across-the-board tax rate cuts if Louisiana's economy meets specific benchmarks. The decision to cut (or raise) taxes should rest with the Legislature and governor, and not be determined by a formula that could result in Louisiana having less revenue available for basic necessities.

- Enact a tax on inherited wealth. The Center on Budget and Policy Priorities estimates that Louisiana could raise $70 million a year by reinstating its tax on estates worth more than $3.5 million.

Corporate

- Increase tax compliance by large corporations by enacting combined reporting.

Sales Taxes

- Broaden the sales-tax base to include services taxed in Texas and other Southern states.

- Reduce vendors' compensation.

Other

- Raise Louisiana's gasoline tax, which has lost more than half of its purchasing power since the last time it was increased 33 years ago.
- Amend the constitution to end the supermajority requirement for revenue increases. It only takes a majority vote to cut funding for schools or health care services, and Louisiana should have the same threshold for raising revenue.
- Tax recreational marijuana.
- Consider raising the excise tax on beer, liquor and tobacco.

Above all, the Legislature should remember the lessons of the recent past, and avoid the election-year temptation to make permanent tax cuts during a temporary economic surge. We saw the results of such folly in the years after Hurricane Katrina, when Louisiana's economy boomed and the Legislature moved aggressively to cut taxes on middle and upper-income households. Those tax cuts, on the eve of the Great Recession, were the precursors to a decade of chronic budget shortfalls that led to historic disinvestment in higher education and helped put Louisiana farther behind its regional peers on many indicators of economic well-being.

Louisiana's economy has enjoyed a strong recovery from the economic downturn caused by the Covid-19 pandemic. But much of this economic surge is due to federal pandemic aid that is expiring, and many economists expect the nation to fall into recession in the near future. When that day comes, the job of balancing the state budget while maintaining vital services will become much more difficult.

The best time to prepare for that downturn is now, and the way to do it is by restructuring our tax system to make it more fair, adequate and sustainable for years to come.