

LOUISIANA'S OPPORTUNITY

Comprehensive Solutions for a Sustainable Tax and Spending Structure

Prepared by
The Task Force on Structural
Changes in Budget and Tax Policy

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Summary of Task Force Recommendations [\[Top\]](#)

The Task Force on Structural Changes in Budget and Tax Policy started with the premise that a tax structure should generate sufficient revenues to fund legitimate and necessary government expenses. In so doing, the tax structure should be fair, simple, competitive with other states, and stable over the short and long term. These qualities are best achieved with taxes that are broad-based with low rates, and that do not play favorites for or against a particular constituency. The Task Force viewed economic competitiveness and comparisons to other states as fundamentally relevant factors in its decision making, while attempting to assure that compliance with a new structure would be easy and clear. The Task Force also believes that exceptions should be minimal and for clearly established reasons that serve our state's needs.

The Task Force acknowledges that much of what the state spends each year is constitutionally and statutorily obligated before the Legislature begins the budget debate and is primarily required to meet fundamental state obligations. The Legislature is limited in its ability to alter the spending obligations and there are few clearly identifiable areas that can easily be eliminated to materially reduce overall state spending. Additionally, a substantial portion of the state budget is derived from federal matching funds that cannot be used for anything other than the designated purpose. However, there are areas that should be addressed to provide for better budgeting practices and to prevent overspending, that would mitigate the potential for mid-year deficits, allow for better long-term planning and potentially free up revenues to address long-standing accumulated state obligations.

The Task Force offers the following recommendations that should be considered as a package. Although the changes will require separate pieces of legislation, they should be considered in their entirety as a whole and not individually in isolation, because of their interactions with one another in establishing a balanced and fair tax system. With that in mind, the Task Force - after more than six months of information gathering and deliberations - makes the following recommendations:

Budget and spending recommendations

1. Avoid budgeting practices that allow for spending beyond available recurring revenues.
2. Implement and adhere to improved revenue-needs forecasting, particularly with regard to the MFP, Medicaid and TOPS, that more closely predicts actual utilization. The state should strengthen current law which provides for estimating conferences in various major spending areas to provide a formal multi-year spending forecast for such things as Medicaid, the MFP, TOPS and Corrections.
3. Continue the ongoing review of state contracts to identify opportunities for consolidation, renegotiation or elimination.
4. Examine individual constitutional dedications to determine if they remain a state policy priority.
5. Conduct a holistic review of state trust funds for possible revision, elimination or merger of funds.
6. Continue to implement fiscal structures that will help protect the state budget from swings in volatile state revenue streams, such as mineral revenues and corporate taxes.

7. Implement staggered sunsets on all statutory dedications to see if they can be adjusted, eliminated or combined with others.
8. Continue payments to state pension systems on the initial Unfunded Accrued Liability under the current timeline to avoid increasing debt, while looking for ways to accelerate payments toward an earlier debt retirement.
9. Examine expected rates of return on pension investments to make proper adjustments to ensure that the retirement systems are not creating another new and costly unfunded accrued liability in the future.
10. Continue review of various tax credits, rebates, deductions, and exemptions to state taxes to determine whether they can be eliminated, curtailed or more closely regulated.

Sales tax recommendations

1. Expand the sales tax base and reduce the sales tax rate from its current 5% to no more than 4%. To do so, the Task Force recommends: (1) retaining, with a few modifications, the expanded state sales tax base adopted in Act 26 of the first special session of 2016 and amended by Act 12 in the Second Special Session, which would continue the tax on such things as custom software, business utilities, and storm shutter devices; and (2) making certain services, such as those taxed in Texas, and digital transactions subject to sales tax. Some of the taxable services include cable and satellite television, repairs to nonresidential, commercial property, web hosting and security services.
2. The state should take meaningful steps to establish a more uniform sales tax base by bringing exemptions and exclusions in line on both the state and local levels.
3. State and local governments should work to create a uniform system of tax administration, collection and audit that respects and protects local revenue streams from any overlap with state revenues.
4. Give local governments the authority to increase their sales tax rates without a vote of the state Legislature, but still require a vote of the people in the area being taxed. Sales tax and property tax reform are essential if local governments are to have the tax capacity to independently provide their own funding.
5. In order to provide greater clarity and ease of compliance, the Task Force recommends a recodification of sales tax law.

Income tax recommendations:

1. Eliminate the state deduction for federal income taxes paid, accompanied by appropriate state income tax rate reductions. This change would decouple Louisiana's income tax base from federal tax changes. Eliminating federal tax liability as a deduction for the income tax will break the connection between federal changes in tax policy and state income tax collections. The state should not be rewarded when the federal government decides to lower taxes nor penalized when the federal government decides to raise federal taxes. The only way to lower the individual income tax rates is to get rid of the federal tax liability exemption. It also recommends limiting the excess itemized deduction for personal income to 50%. These two deductions account for a reduction of \$1.225 billion in income tax collections in Louisiana at the current rate structure. These exemptions provide a much larger tax break to higher income groups, both absolutely and proportionally. If the excess itemized deduction were limited to 50%, mortgage interest and charitable giving would still be deductible. This proposal, along with the state's reliance on the sales tax, will balance the overall tax structure among various income categories in terms of who is paying for state services.
2. Two options for changes to the individual income tax law _ one constitutional and the other statutory. A constitutional option allows Louisiana to expand the income tax base, narrow the brackets, and lower all rates by 25%. A statutory option only allows base expansion and narrowing

of the brackets.

a. Under the constitutional option, the Task Force recommends allowing voters to approve the elimination of the federal income tax deduction that decouples the Louisiana tax base from federal tax changes. This option would include scaling back excess itemized deductions to 50%. A new three-bracket structure would be used and rates of taxation lowered – 1.5% on the first \$25,000 (\$12,500 single), 3% on \$25,000 through \$50,000 (\$12,500 through \$25,000 single) and 4.5% above \$50,000 (above \$25,000 single). Not only would rates be lowered by 25%, but they would apply more fairly and evenly to all taxpayers because of the proposed elimination of many deductions and exemptions.

b. Under the statutory option, the excess itemized deduction would be fully eliminated. This would be coupled with the elimination of other deductions and exemptions proposed by the Task Force. The statutory option would use the new compressed three-bracket structure, but tax rates would remain at the current 2%, 4% and 6% levels.

3. Eliminate many income tax exemptions and credits and impose a moratorium on any new tax credits or exemptions applied to the individual income tax. The Task Force recommends keeping (1) the standard and dependent deductions, (2) the exclusion for military pay for active duty personnel, (3) the credit for taxes paid to another state, (4) the earned income tax credit (because it allows the state to enhance the progressivity of its income tax and reduce the regressive nature of the overall state tax structure), (5) the exclusions for social security and retirement income for public employees, and (6) credits related to child care and early childhood education (in part because these programs help all families and improve educational outcomes, and in part because they leverage federal money).

Corporate tax recommendations:

1. Eliminate the deduction for federal taxes paid for the corporate income tax. A constitutional amendment included on the statewide ballot on Nov. 8, 2016, failed with 44% of voters favoring the amendment. The reform would have decoupled the Louisiana tax base from federal tax changes and would have set the corporate tax rate at a flat 6.5%. The upper bracket rate for Louisiana currently is 8%. This approach would have better aligned Louisiana with its competitor states, potentially provided for a more stable source of revenue than the current corporate income tax structure, and eliminated instability in state corporate tax collections due to actions in Washington, D.C. The Task Force believes this proposal should be considered again since it will be impossible to lower the marginal corporate tax rate, a very important ingredient in long-term tax reform, without eliminating a major exemption such as federal tax liability. Also, at this stage, it will be combined as part of an overall tax reform package reform and hopefully will be backed by political leaders with a strong constituency of support. A convincing public education effort will be needed.

2. Direct the Department of Revenue, with the Louisiana Tax Institute, to study moving from singleentity taxation on the corporate level to a system of combined reporting with findings due by January 2019. Under combined reporting, corporations are taxed based on their apportioned share of income of their “unitary group” which includes a variety of criteria, including common ownership, common management and common lines of business. Combined reporting solves the profit-shifting incentive because related companies are part of a unitary group in which intercompany transactions are eliminated. Instead a state will apportion the entire unitary group using a combined return to determine its share of its tax base.

3. Restructure, phase out or eliminate the corporate franchise tax, provided the state identifies replacement revenue that coincides with changes in the tax. The analysis of the restructuring, elimination, or phase out, along with the identification of the replacement revenue source, is to be conducted by the Department of Revenue, with the Louisiana Tax Institute. The findings are to be

presented to the Legislature by January 2019.

Ad valorem tax recommendations

1. Amend the Louisiana Constitution to provide local governmental authorities with a role in granting industrial tax exemptions and create a statutory framework to establish the extent of this role for local involvement, as well as defined policies for use of the exemption as an economic development tool that favors job growth.
2. Expand the use of payment in lieu of tax arrangements for local governments considering property tax exemptions to attract economic development. Such arrangements should require the coordinated approval of the elected officials in the impacted taxing jurisdiction.
3. Amend the Louisiana Constitution to allow for a gradual elimination of locally-imposed inventory taxes over a 10-year period accompanied by the elimination over a five-year period of the state income and franchise tax credit paid on inventory. To offset local governments' reduction in revenues, the Task Force suggests several options, including a constitutional change to allow a rollup in existing property tax millages, enhanced local revenues resulting from expansion of the sales tax base and changes to the industrial tax exemption, and creation of a temporary revenue sharing fund to bridge the gap as the inventory tax goes away.
4. Amend the Louisiana Constitution to limit the property tax exemption on property owned by nonprofits to that used exclusively for the tax-exempt purposes of the non-profit.

Economic development incentive recommendations

1. Require the Louisiana Department of Economic Development (LED) and the Legislature to establish sunset review periods for all incentive programs and eliminate underutilized or inactive programs.
2. Require LED to continue to monitor and regularly report on the performance of all its incentive programs. The reporting must include information on the return on investment for each program and be conducted by independent third parties in accordance with the legislatively established objectives for these programs.
3. Retain the Motion Picture Investor Tax Credit as a non-appropriated, non-refundable tax credit incentive with both discounted redemption and transferability as alternative options for use. The Legislature should implement a modified front-end cap to control the number of credits issued from inception and implement other mechanisms to encourage reasonably timely use to avoid the creation of another backlog of credits that would put a drain on the state budget. The implementation of the front-end cap should coincide with the elimination of the back-end cap.