

## CHAPTER 4. PUBLIC INVESTMENTS, TAXES AND STATE REVENUE

**Key Takeaways:** Employers and workers alike need quality and accessible K-12 and higher education systems, strong infrastructure, safe communities and other building blocks for creating jobs and growing prosperity. The 2007 recession caused sharp declines in the state revenues available to invest in economic growth, and revenues are still well below pre-recession levels. Lawmakers' response to the revenue shortage thus far has centered mainly on reducing investments, but a more prudent course would be to maintain investments in education, roads and healthcare through a balanced approach that includes revenue increases rather than take a cuts-only approach that threatens recovery.

Updating the state's tax code would improve the equity of the state's tax system for its workforce and provide resources necessary to attract business. Overall, Mississippi's state and local tax systems call on low- and moderate-income people to pay a higher share of their yearly earnings in taxes than high-income individuals. Addressing this imbalance would help raise the money needed to invest in economic growth and do it more equitably.

Taxes are important to working Mississippians not just because they represent a portion of their paychecks, but also because they fund the public structures that provide the foundation for creating jobs and building a strong economy. Employers and workers alike need quality and accessible K-12 and higher education systems, strong infrastructure and safe communities. These structures require adequate resources. Taxes should be equitable and structured based on a worker's ability to pay. Beyond tax structure, transparency is also necessary to make sure the public is getting the most out of economic development efforts, many of which are administered through the tax code.

### MISSISSIPPI TAX SYSTEM

The taxes that Mississippi collects from individuals and businesses include:

- Income taxes, which are a percentage of individual and business yearly earnings;
- Sales and use taxes, which are a percentage of the price of goods and services purchased in the state; and
- Special taxes on certain businesses (e.g., casinos) and goods (e.g., gasoline).

In FY 2010, Mississippi collected \$6.56 billion in state taxes. *Figure 19* shows Mississippi's tax revenue collections by source in FY 2010.

As shown in the figure, sales and use taxes made up the largest portion of state tax revenue at 44%. The second largest revenue stream was the personal income tax, which made up 26% of state revenue. The corporate income tax made up 7% of state tax revenue.

### ADEQUACY

An adequate tax system is needed to maintain public investments (such as education, infrastructure, and public safety) that support the state's workforce. The adequacy of state resources in Mississippi was a challenge even before the recent recession and continues as significant budget cuts threaten the state's public structures. Compared with other states, Mississippi ranked 46th in taxes per capita, the average amount collected per person through all tax sources. *Figure 20* shows each state's per capita tax collections in FY 2009 (the latest data available from the U.S. Census).

### MISSISSIPPI TAX COLLECTIONS BY SOURCE FY 2010

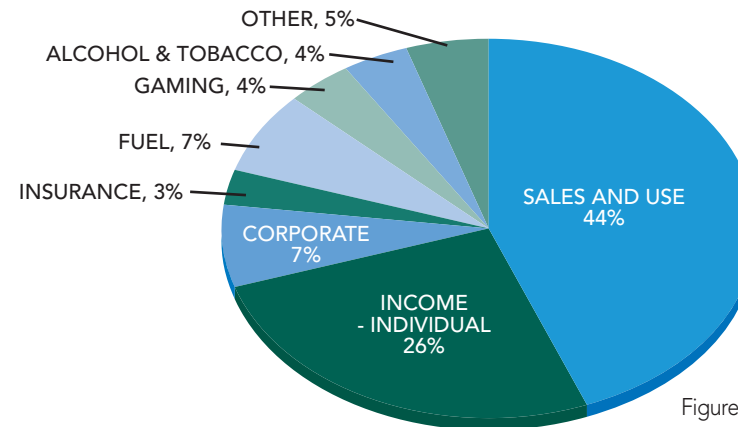
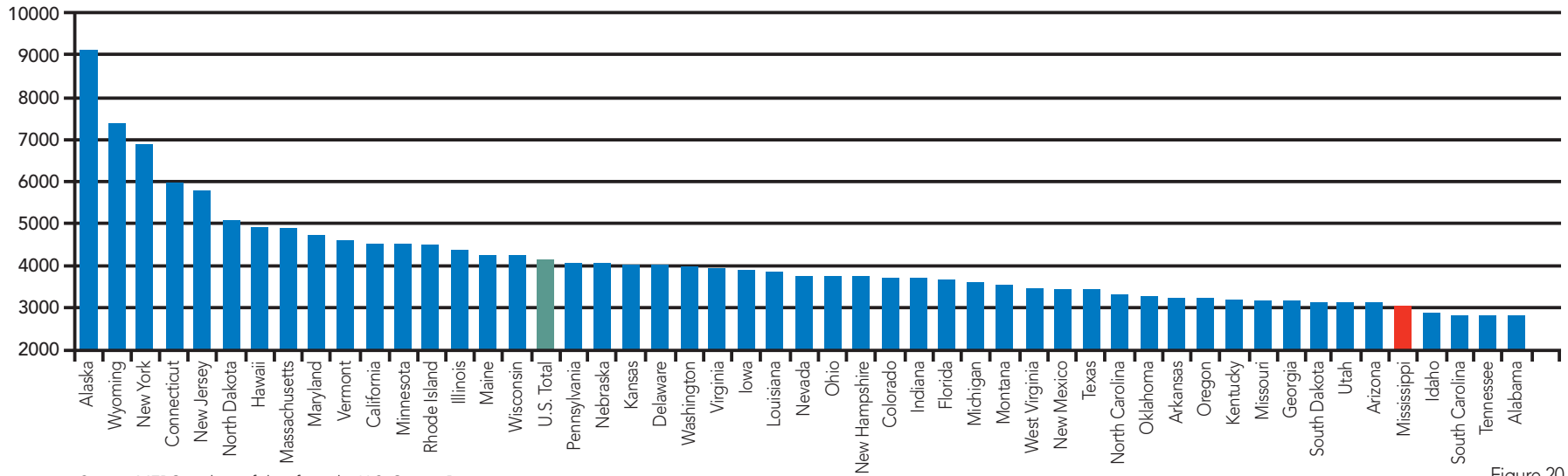


Figure 19

Source: MEPC analysis of MS Department of Revenue Annual Report FY 2010 data

## STATE AND LOCAL TAXES COLLECTED PER CAPITA BY STATE IN FY 2009



Source: MEPC analysis of data from the U.S. Census Bureau

Figure 20

The 2007 recession triggered a sharp decline in state revenue, and revenues are still well below pre-recession levels. *Figure 21* shows general fund revenue collections during and following the recession.

FY 2008, when revenues peaked after the boost to the state's economy from recovery spending following Hurricane Katrina, was the last year that the state has been able to fully fund the Mississippi Adequate Education Program, the funding formula for all of Mississippi's K-12 schools.

While federal American Recovery and Reinvestment Act funding helped the state avoid more drastic cuts during and after the 2007 recession, it did not cover the total shortfall. Lawmakers dealt with the revenue shortages with year after year of cuts to essential services. These cuts caused, among many other things, increases in some K-12 class sizes, tuition hikes at state universities, and a reduction in mental health services.

## MISSISSIPPI GENERAL FUND REVENUE COLLECTIONS FY 2008-FY 2013

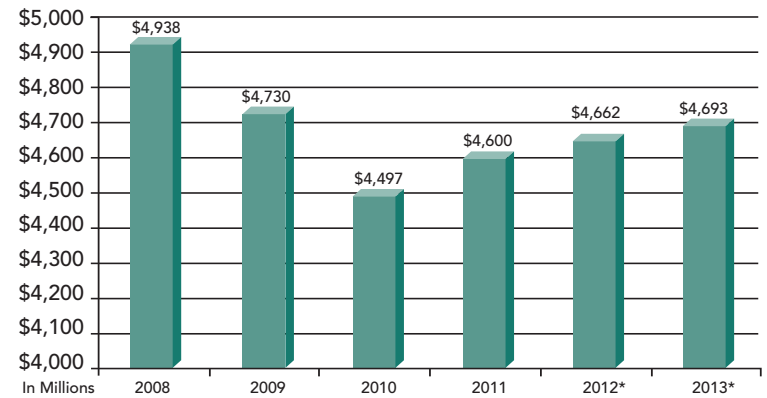


Figure 21

\*Indicates the revenue collection amount is an estimate

Source: MEPC analysis of data from the Mississippi Revenue Estimating Group

## TAX EQUITY

Tax reform is also necessary to improve the equity of the state's tax system for working Mississippians. While Mississippi's tax system has both progressive and regressive elements (see definitions in Key Terms box), as a whole the state's tax system is regressive. Earners with lower incomes (less than \$39,000 per year) pay over 10% of their income in state and local taxes, while those earning over \$70,000 pay less (see figure 22). The top 1% of earners (those earning \$319,000 or more annually) pay only 6.3% of their income in taxes.

### DEFINING KEY TERMS

**Regressive Tax Structure:** A tax system is regressive if persons with lower incomes pay a higher percentage of their income in taxes than those with higher incomes.

**Progressive Tax Structure:** A tax system is progressive if persons with higher incomes pay a greater percentage of their income in taxes than those with lower incomes.

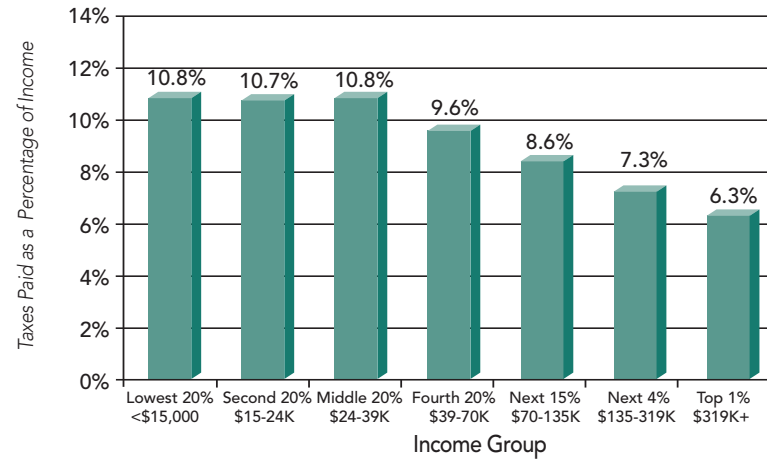
Two key features cause Mississippi's tax system to be regressive overall:

- A heavy reliance on the sales tax, which takes a higher percentage of lower income residents' earnings than it does from the high-income residents. The discrepancy is made worse due to the sales tax's inclusion of groceries and exclusion of many services that are less frequently used by low- and moderate-income households. Mississippi is one of only two states (Alabama is the other) that extend the full sales tax to groceries without any offsetting credits. In contrast, many services, including pet grooming and massage services, are not taxed.
- An effectively flat income tax with a top bracket that starts at \$10,000 of taxable income. With standard exemptions and deductions, a family of four would begin to owe income taxes at \$19,600 in income, even though their income is below the federal poverty level. That same family of four, if they earned just \$10,000 more, would enter the top bracket at \$29,600 and pay the highest tax rate on income above that threshold. Families making \$30,000 or \$3,000,000 are in the same tax bracket.

The regressive tax structure exacerbates the state's already significant income inequality. Income tax brackets have not been updated in more than 25 years. During that time, persons with higher incomes experienced substantial income gains compared with low-income residents. Figure 23 shows income growth by income group over the last two decades.

The top 20% of earners have experienced more than twice as much income growth as earners in the bottom and middle groups. In order to capture this growth and make the income tax more progressive, a new, higher bracket should be added to the state's income tax. Adding a new income tax bracket would also raise revenue to fund services needed to build Mississippi's economy.

## ESTIMATED PERCENT OF INCOME PAID IN STATE & LOCAL TAXES BY INCOME QUINTILE IN 2007



Source: MEPC Analysis of Data from the Institute on Taxation and Economic Policy, "Who Pays? A Distributional Analysis of the Tax Systems in all 50 States," November 2009.

Figure 22

## MS INCOME GROWTH IN THE LAST TWO DECADES BY INCOME GROUP

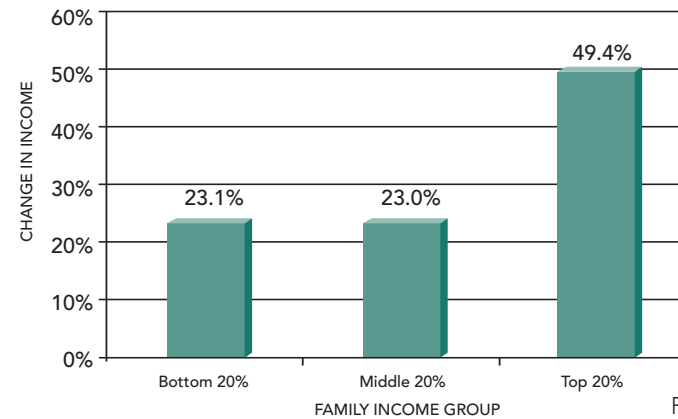


Figure 23

Source: Center on Budget and Policy Priorities, "Pulling Apart: A State by State Analysis of Income Trends," April 2008.

**Note:** This chart includes income data through the mid-2000s but does not include income data from the recent recession. Income disparity may have widened further due to the recession.

## TRANSPARENCY

Many of the state's economic development programs, which are designed to attract corporations to do business in the state, are administered through the income tax code as tax exemptions or tax credits. In addition to the personal income tax, the state collects a corporate income tax on business profits. A corporation's income tax liability may be reduced by one of many allowed deductions or one of the state's many corporate tax credits. In Mississippi, tax credits are provided to corporations for a wide variety of actions, including creating new jobs, providing child/dependent care for employees, and producing motion pictures in the state.

Partly due to these deductions and credits, most corporations in Mississippi pay no income tax. Research from the state legislature's Performance Evaluation and

Expenditure Review Committee in 2011 found that approximately 80% of corporations operating in Mississippi pay no state corporate income tax, and close to 70% of the state's largest corporations pay no income tax.<sup>xv</sup>

While these tax credits are enacted to support a public purpose (i.e., economic development), for many of them data is not available to allow for review of the tax credit's effectiveness. For example, the Jobs Tax Credit has provided corporations with tax credits between \$5 million and \$20 million annually for the last three years, but data is not available on the number of jobs created by the tax credit. These kinds of data are necessary to evaluate the effectiveness of these credits. Public access to these data would make the tax system more transparent.

## RECOMMENDATIONS

Public investments should provide a quality education for all students, a healthy workforce and an infrastructure for business development that creates more jobs with quality wages. As Mississippi's leaders seek ways to strengthen the state's workforce in the wake of the recession, they should include ways to increase revenues that would lift Mississippi and its workforce to greater economic competitiveness while improving the tax system's equity.

- **UPDATE THE INCOME TAX** to create higher income tax brackets and make the tax more progressive. A new rate of 6% on taxable income over \$45,000 (which is \$64,600 of total earnings for a family of 4) and 7.5% on income over \$100,000 would bring in an estimated \$117 million through the personal income tax and \$150 million through the corporate income tax.
- **BROADEN THE SALES TAX** to include more services. Including 21 new services in the sales tax as recommended by the Governor's Tax Study Commission would bring in an estimated \$98 million, and including all services used by households would bring in an estimated \$287 million annually.
- **CLOSE CORPORATE INCOME TAX LOOPHOLES.** While there is no publicly available estimate of the amount of money lost to corporate tax loopholes, the measure would bring in additional revenue and make corporate taxes more fair for local businesses.
- **REQUIRE MORE REGULAR REVIEW** of corporate tax credits and provide information to the public in order to determine whether the tax breaks really create jobs and help the economy.

xv Performance Evaluation and Expenditure Review, letter to Representative Cecil Brown dated January 18, 2011