Policy Brief

All Roads Lead to Nowhere:

Big Tax Cuts are Unaffordable and Do Little for Working Families

MEPC A Hope Initiative
Mississippi Economic Policy Center

MEPC A Hope Initiative
MISSISSIPPI ECONOMIC POLICY CENTER

All Roads Lead to Nowhere:
Big Tax Cuts are Unaffordable and Do Little for Working Families

Big tax cuts that largely benefit corporations and wealthy Mississippians are unaffordable and will erode our ability to support schools, universities, roads and bridges and public safety. Big tax cuts will undermine our future by making it harder for the state to invest in the things that make Mississippi's working families more productive like a high-quality public education system, access to health care and making college affordable.

The high cost of big tax cuts may require Mississippi to raise revenue in the future through higher sales and property taxes, both of which hit lower and middle income earners hard. The end result will be worsening schools and roads and a tax shift away from the wealthy and onto lower and middle income families.

In contrast, targeted tax relief, like a refundable Earned Income Tax Credit, would help working families who are struggling to make ends meet, is more affordable, and will help the economy more than the other proposals under consideration.

Time for a tax cut?

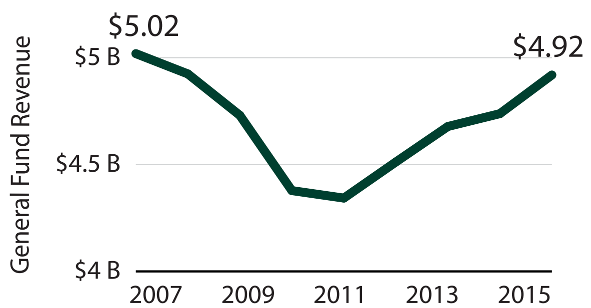
Mississippi's state budget looks better than it has in quite a while. Revenues are increasing and the state's rainy day fund is full. However, the state is still climbing out of the deep hole caused by the recent recession.

Despite recent progress, K-12 school funding is still down $623 per student since before the recession, and there are 2,250 fewer teachers in the classroom. Mississippi's universities have seen their funding cut 25% per student, and tuition has been raised accordingly, making a college education unaffordable for more people. One in five bridges in the state needs to be repaired or replaced. Rural hospitals in the state are struggling to make payroll and keep their doors open because the state has failed to make investments in healthcare.

State Revenue Still Recovering
Increase Not a Surplus

While in the short term it seems like revenues have been increasing, in reality they are still recovering from the deep trough caused by the recession.

IN 2009 DOLLARS



Source: MEPC analysis of data from the Legislative Budget office and the U.S. Bureau of Economic Analysis
MISSISSIPPI ECONOMIC POLICY CENTER

As revenues continue to recover, we can start making progress towards better schools, bridges, health care, and more. Tax cuts would not only jeopardize our recent progress but also our ability to make progress in the future.

The details and the costs

Currently there are two major tax cut proposals being considered by the Mississippi Legislature, one from each chamber. The Senate plan would phase out the corporate franchise tax and the 3% income tax bracket, and add a self-employment tax deduction. The House plan would phase out the personal income tax.

Senate Plan—SB 2839

The Details:
- Phase out corporate franchise tax in 10 years
- Phase out 3% personal and corporate income tax bracket in 5 years
- Allow deduction on state income taxes equal to 50% of federal self-employment taxes paid (i.e. Social Security and Medicare taxes)

The Cost:
- $234 million in five years
- $380 million when fully phased in

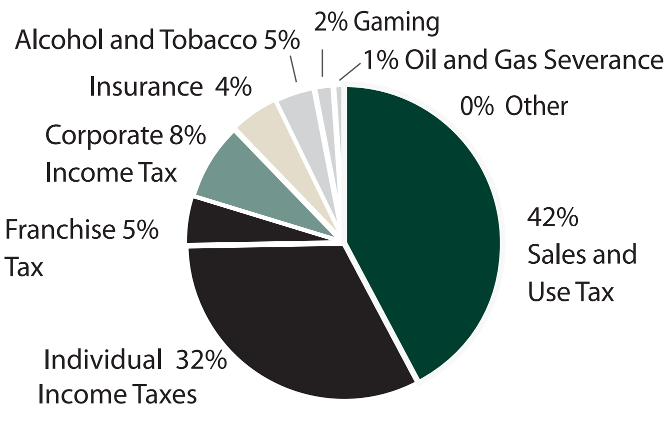
House Plan—HB 1629

The Details:
- Phase out personal income tax over 15 years
- It first eliminates the 3% bracket, then the 4% bracket, and then the 5% bracket
- Does not apply to corporate income tax
- Phase out plan only advances in years with 3% revenue growth

The Cost:
- $183 million in five years
- Roughly 1/3rd of state tax revenue once fully phased in (currently $1.7 billion)

Individual income taxes are Mississippi's second largest revenue source behind sales taxes, bringing in about $1.7 billion annually and making up almost one third of all general fund dollars that support schools, universities, mental health resources, public safety, and other key services.

State Tax Revenue Sources
General Fund



Total: $5.25 billion

Source: MEPC analysis of data from the Legislative Budget Office and Department of Revenue
MISSISSIPPI ECONOMIC POLICY CENTER

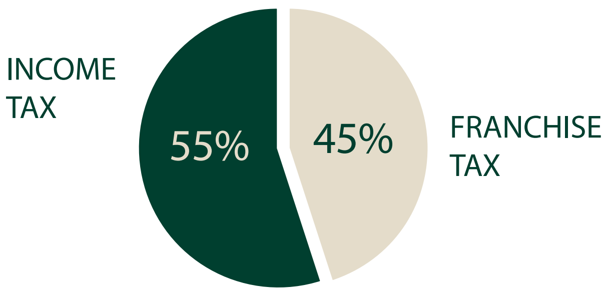
More cuts for corporations

By phasing out the income tax, Mississippi will see significantly less in tax revenue than it would have otherwise. That means the state will have less funding for pulic education, public safety and repairing the state's roads and bridges. Just as important, eliminating the income tax will not generate the additional economic activity needed to cover the loss in revenue – in other words, the tax cut will not pay for itself. The state depends on revenue growth to cover increasing costs like gas for school buses, asphalt for roads, wages and benefits for teachers, state troopers, and other state workers, health care, and increased costs for others goods and services.

While the elimination of the income tax is the most drastic of these measures long-term, the Senate plan should not be viewed as an affordable alternative. In fact, in the first five years the Senate plan would cost $50 million more than the House plan, causing real damage to schools and other services people rely on every day. The franchise tax phase out, elimination of the 3% income tax bracket, and the self-employment tax deduction will cost $234 million annually in the first five years and $380 million annually when fully implemented in ten years.

Franchise Tax = Large Portion of Corporate Tax Revenue

CORPORATE TAX REVENUE SOURCES 2010-2014



Source: MEPC Analysis of data from the Mississippi Department of Revenue Annual Reports

MISSISSIPPI ECONOMIC POLICY CENTER

The Senate plan, in addition to the individual income tax cuts, would also cut taxes for corporations in two ways. First, in eliminating the 3% income tax bracket, it would benefit corporations paying income taxes, in addition to individuals. Second, it would phase out the state's corporate franchise tax over 10 years.

The franchise tax charges corporations $2.50 on every $1,000 of capital or property invested in the state. For the past five years, franchise tax collections have averaged about $220 million annually, bringing in $242 million in 2014. While it doesn't often garner a lot of attention, the franchise tax is not an insignificant corporate tax ; it makes up almost 45% of corporate tax collections.

To put the amount of franchise tax collected in perspective, it is roughly equal to what we invest in our community colleges, which train and educate workers, or what we spend to help those suffering from devastating mental illnesses. It is almost four times what we spend on our state troopers to help keep us safe or on preventing the spread of disease.

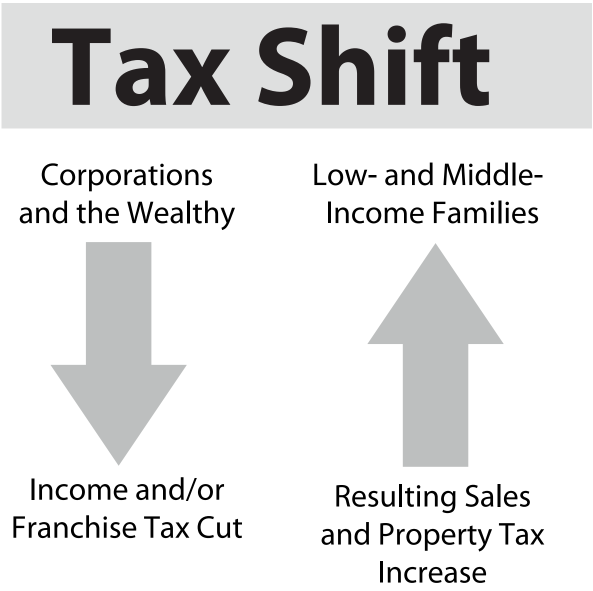
Many corporations paying franchise taxes pay little or no income taxes. Under current corporate income tax law, 60% of corporations pay zero state income taxes and 83% pay less than $150 annually. Those who pay $150 or less would pay zero if the 3% income tax bracket is phased out.

Corporate tax cuts are often incorrectly touted as an easy way to make a state attractive to businesses. This legislative term alone (2012-2015), the legislature has enacted many corporate tax breaks based on this, ranging from credits on inventory taxes to fuel tax reductions to reduced penalties for non-payment of taxes.

In a recent ranking by Forbes Magazine, the "Best States for Business", Mississippi ranked near the top one-third for states with the best business costs, which took into account taxes. But businesses make decisions based on many other variables, and Mississippi is doing poorly in those areas. Mississippi ranked lowest in critical areas like well-trained workers and quality of life — which both require long-term public investment in high quality schools, safe communities and healthier people. The proposed tax cuts will jeopardize the state's ability to make progress in producing a healthy, well-trained and skilled workforce.

Neither tax plan helps working families

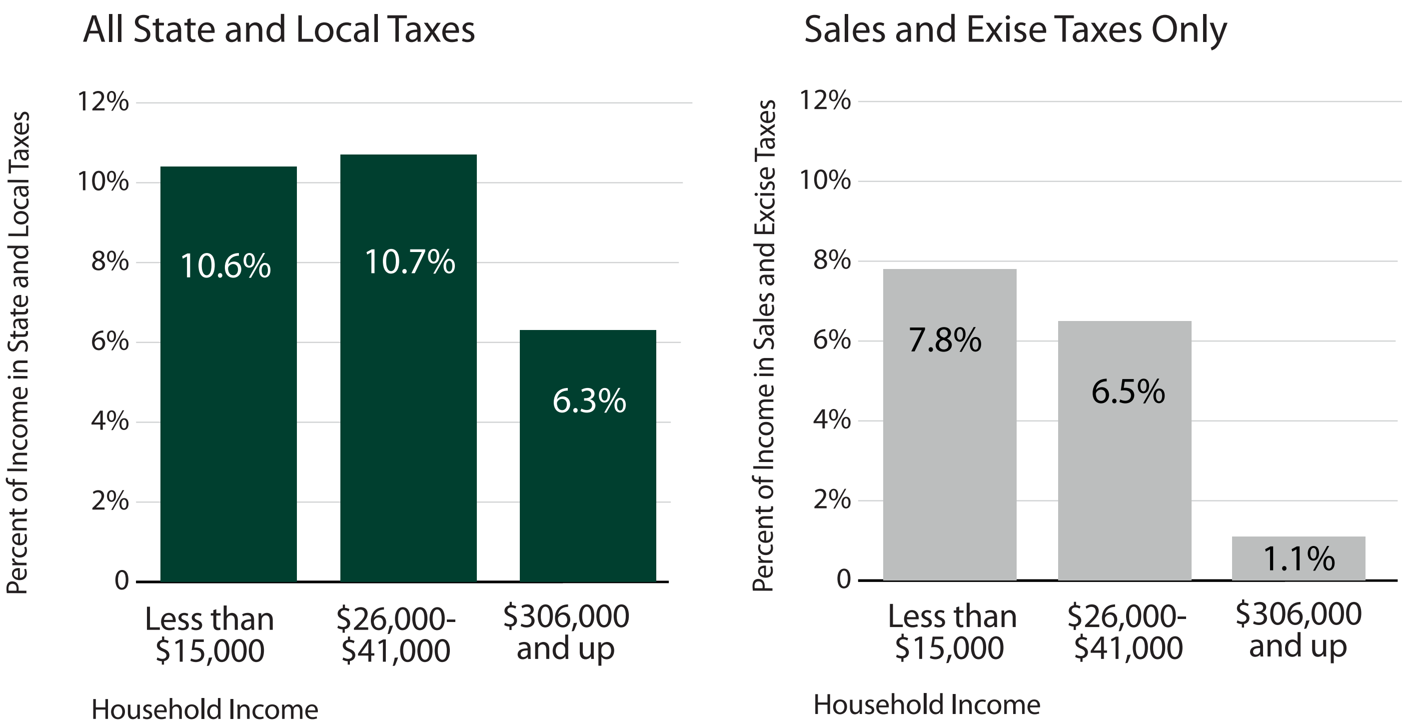
The personal income tax cuts from both the House and Senate plans would benefit wealthier families more than lower and middle income earners. Further, the high cost of these plans may require raising revenue through increases in the property tax or sales tax, both of which hit lower and middle income earners hard. This combination would result in a tax shift from wealthy Mississippians to lower and middle income families.



One reason these plans do not benefit the lowest income Mississippians is because many of them have little to no income tax liability; however, this does not mean they do not pay taxes. Far from it. These families pay a higher percentage of their income in state taxes (mostly sales taxes) than the higher income families these plans benefit most. In fact, lower income families pay more than seven times as much in sales taxes as a percent of their income than the top one percent of households.

Lower and Middle Income Families Pay More

Mississippi's tax system requires families who are struggling to make ends meet to pay more of their income in state and local taxes than wealthy families

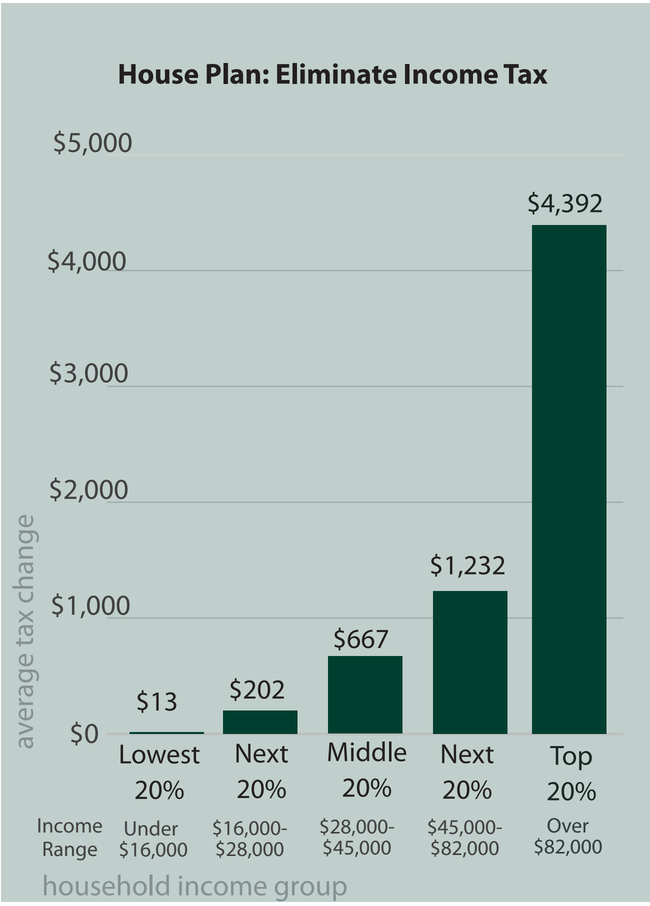


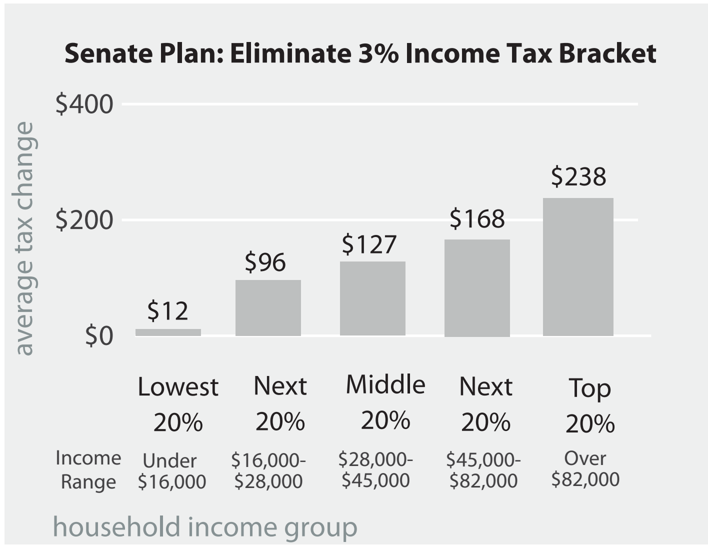
Source: MEPC analysis of data from the Institute on Taxation and Economic Policy for 2015
MISSISSIPPI ECONOMIC POLICY CENTER

House and Senate Personal Income Tax Proposals Benefit the Wealthy

Proposed House and Senate tax cut plans benefit wealthy Mississippians more than low- and middle-income families. However, the Governor's proposed Working Families Tax Credit is more affordable and targets families most in need.

AVERAGE HOUSEHOLD TAX CUT BY INCOME GROUP





Source: Institute on Taxation and Economic Policy

MISSISSIPPI ECONOMIC POLICY CENTER

One alternative to these tax cut plans, is to enact a state Earned Income Tax Credit (EITC). A state EITC would provide targeted tax relief to working families who are struggling to make ends meet. It is also more affordable for the state, and by putting money directly into the hands of families who will spend it in their communities it will help local economies more than the other tax cut proposals.

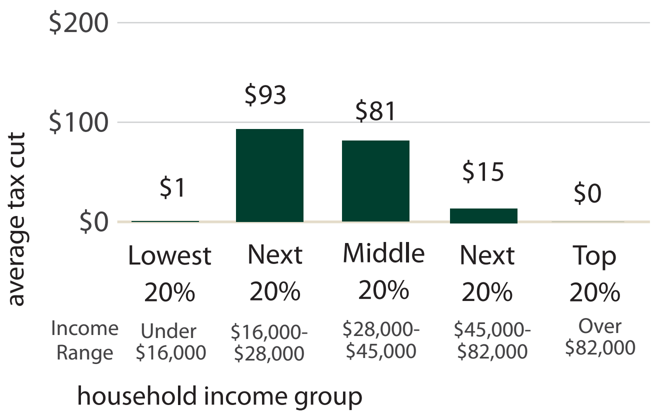
Governor Phil Bryant took this approach when he proposed the Working Families Tax Credit. The Working Families Tax Credit would give working families earning below $52,000 a tax credit equal to 15% of the federal EITC.

Making this proposed credit refundable would allow it to go even further to help the working families who need help the most. An 8% refundable credit would cost approximately the same as the estimated cost for the 15% non-refundable credit, about $79 million.

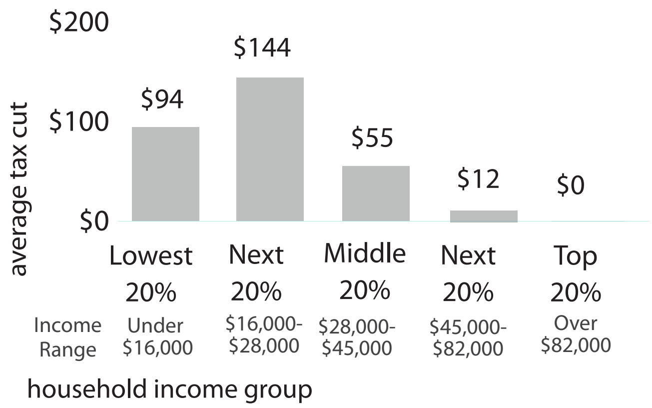
A State Earned Income Tax Credit: Targeted, Affordable Tax Relief

Proposed by Governor Bryant through the Working Families Tax Credit, a state Earned Income Tax Credit would provide targeted tax relief for the working families who need it most. Because it is targeted, it is more affordable than the other tax cut options being considered. A 15% nonrefundable tax credit like the one proposed by the Governor is estimated to cost $79 million. An 8% refundable credit would cost the same amount and offset not only income taxes but some other taxes, like sales taxes.

15% Earned Income Tax Credit, Nonrefundable



8% Earned Income Tax Credit, Refundable



Source: Institute on Taxation and Economic Policy
MISSISSIPPI ECONOMIC POLICY CENTER

Conclusion

A drastic tax cut, like both of those proposed in the House and Senate, will not boost our economy. States promote real, long-term economic growth by investing in quality schools to educate a skilled workforce; a modern infrastructure that enables companies to bring their products to market; and safe, stable communities. All of these things require long term public investment that would be jeopardized with a big tax cut.

We can all agree that we want our state to be competitive and add jobs, but big tax cuts are not what we need to build our economy. Mississippi's weaknesses lie in the fact that we have not maintained sufficient investment in the things that would make our workforce productive. As Mississippi positions itself to become more competitive in growing its economy, the state should center its focus on continued investment in an educated, healthy and well-trained workforce instead of big tax cuts that largely benefit corporations and wealthy Mississippians.

Other States Have Been Down This Road

Throughout the country lawmakers are looking for easy answers to spur economic growth in their states, often touting large tax cuts that mainly benefit corporations and wealthy residents.

States like Kansas, Wisconsin, Pennsylvania, and North Carolina have recently passed sweeping tax cut measures, but their results are ranging from disappointing to devastating. Many of these states now have budget problems akin to those that occurred during the recession.

The biggest of these tax cuts have happened in Kansas, and they are now feeling the consequences. The Kansas cuts have been even more costly than expected, eating up the state's reserve funds and causing credit rating downgrades, without producing any of the promised quick economic gains. In fact, since the cuts went into effect, Kansas has added jobs at a slower rate than the rest of the country. Making matters worse, it has led to huge funding cuts to public schools and universities, with more cuts to come this year.

Mississippians do not have to look as far as Kansas to see the harmful consequences of tax cuts. Neighboring Louisiana has a $1.6 billion budget shortfall this year and had to make mid-year cuts in six of the last seven years since enacting tax cuts.

MEPC A Hope Initiative
MISSISSIPPI ECONOMIC POLICY CENTER

The Mississippi Economic Policy Center (MEPC) is a nonprofit, nonpartisan organization that conducts independent research on issues affecting all Mississippians. MEPC uses its analysis to inform the policy dicussion and create economic opportunity for people and communities who need it most. MEPC is an initative of HOPE.

HOPE (Hope Enterprise Corporation and Hope Credit Union) provides affordable financial services; leverages private, public and philanthropic resources; and engages in policy analysis in order to fulfill its mission of strengthening communities, building assets and improving lives in economically distressed parts of the Mid South.

MEPC A Hope Initiative
MISSISSIPPI ECONOMIC POLICY CENTER

4 Old River Place
Jackson, MS 30202