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Time for new revenue? Tax advocates seek to 'balance' budget cuts

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With each passing round of information updating the state's fiscal outlook, the goal of building a Mississippi with quality schools, state-of-the-art transportation and safe communities appears to be more out of reach than it was before the recession.

By 2012, Gov. Haley Barbour projects that the budget gap could reach $1.2 billion. For the foreseeable future, Mississippi will have significantly less money than in past years to educate children, to train the work force and to build the infrastructure that fosters business development.

In light of the fiscal outlook, the Mississippi Economic Policy Center (MEPC) authored a piece in the Perspective section of The Clarion Ledger last fall titled "Commentary on Mississippi's fiscal woes: Are tax hikes on the table?" In the commentary, MEPC outlined four reasons to support a balanced approach that included raising revenues:

- Mississippians most in need will be those hurt the most. This scenario is playing out as class sizes are increasing and some schools report kindergarten class sizes as high as 30 children.

- Mississippi has benefited from short-term funding that cannot be sustained under the current tax structure.

- While tax increases and budget cuts both hurt the state's economy, tax increases - especially on those with discretionary income - do less harm than budget cuts which pull money out of the state's economy on a dollar-for-dollar basis.

- Crucial public policy advancements have been made in the state's K-12, work force development and post-secondary structures over the last few years. Most experts agree that for Mississippi to move forward, the educational attainment of our population must increase. It is critical that education reforms at all levels have the resources needed to be implemented successfully.

Given the magnitude of the gap, a balanced approach, that includes raising revenues, merits consideration. Three policy options offer a starting point for discussion on this topic.

Modernize Mississippi's sales tax to reflect the 21st-century economy.

The sales tax was designed during the Great Depression to provide the state with revenue based on what people bought. Back then, people spent most of their money on things rather than services. In recent decades, however, the share of spending that households devote to goods has declined and the share of what households spend on services has increased.

Importantly, a number of services that people purchase today did not even exist when the sales tax was instituted and are exempted from the sales tax (tanning services for example). Those exemptions cost the state money in the form of lost revenue and create some imbalances. For example, if one buys a lawnmower to cut his or her own grass, he or she will pay sales tax on the purchase. However, if one pays a lawn service, he or she does not pay the tax.

Recognizing the trend in purchasing habits, the Mississippi Tax Study Commission appointed by Gov. Barbour in 2008 made the recommendation to "add additional services to the list of taxable services." The recommendation included 21 items ranging from motor vehicle towing to pet grooming. Taxing the services listed in the report would generate an estimated $80 million annually.

Update Mississippi's personal income tax.

Mississippi's personal income tax brackets have not been updated in 25 years. Hence, a family of four with two children earning $30,000 a year is in the same tax bracket as one earning $1 million a year.

Income trends suggest that the current rate structure could be expanded. According to the Center on Budget and Policy Priorities(CBPP), over the last two decades, Mississippians with incomes above $117,000 have experienced over twice the rate of income growth as middle income families earning $40,000.

By adding a new state income tax bracket of 6 percent on "taxable" income over $45,000 (roughly $64,000 a year in "total" income for a family of four including two children), Mississippi could generate approximately $70 million. For taxpayers who itemize on their federal income tax returns, the full brunt of this recommendation would not be felt as many could deduct the state income tax increase from their federal income tax liability.

Update Mississippi's corporate income tax.

Given the link between the personal income tax and the corporate income tax, Mississippi's corporate income tax could also be updated. Estimates conducted by the Institution of Taxation and Economic Policy show that a new 6 percent bracket on corporate taxable income over $45,000 could raise about $55 million annually in Mississippi.

Opponents of a balanced approach that includes raising revenues cite the impracticality of raising revenue during a recession. History, however, provides evidence to the contrary here in Mississippi and nationwide. In response to the 1981 recession, Mississippi lawmakers raised the income tax and the sales tax to preserve the critical investments needed to successfully implement newly passed education reforms.

Likewise, a comparison of the economic performance of states following the 2001 recession shows that in states that raised revenues, growth was not stifled.

Analysis conducted by the CBPP found that states that raised taxes substantially following the 2001 recession "were just as fast to rebound from the recession as states that did not." In fact, in South Carolina, even though the state raised taxes significantly during the recession, personal income and employment grew faster than the national averages from 2004-2007.

Another popular argument against a balanced approach is that businesses will leave or pass over Mississippi for lower taxes. Mississippi's experience, at the very least, raises questions about this argument.

In 2005 Mississippi created the Growth and Prosperity (GAP) Program under which certain types of businesses that located in one of the state's most economically distressed communities could receive sales, income, franchise and property tax breaks for the creation of 10 jobs.

While the benefits of such a program seemed intuitive at the time, the Mississippi Tax Study Commission determined that "GAP is not producing the results that were anticipated when the legislation was established" and suggested "a replacement program that focuses less on tax abatements and more on the other challenges that exist for these targeted areas."

While some notable success stories exist, in the context of our most distressed counties, low taxes are less effective in attracting business development than high-performing schools and a well-trained work force - both of which require investment.

Readers will notice that the revenue recommendations only cover part of the anticipated gap in forthcoming years. The balanced approach recommended is just that - one that balances all strategies for putting together a budget in difficult times: additional revenues, budget cuts, efficiencies and reserves.

The mix of strategies raises questions that are no different than those explored by families during tough times: What can we cut, how can we use our savings while making it last and how can we bring in more income? The balanced approach begins to answer these questions to maintain a high quality of life and to prosper in years ahead.