Commentary
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The Budget is a Real Piece of Work

PAR evaluates the Legislature's tax and spending puzzle as the session enters the final week

As the Legislature attempts to piece together something resembling a balanced state budget, the puzzle that is taking shape is likely to create new problems for state government and require further adjustments during the next year. Lawmakers can be given credit for facing up to some tough decisions this session. But they and the governor contributed to the circumstances over time that led to this crisis situation. Businesses in particular are taking a hit, and it remains to be seen how this will affect the state's improving business climate.

Tax-related legislation this session will create higher net state tax revenue in fiscal year 2016, which begins July 1. While spending cuts are being made in some areas, taxes are going up and the state government will have more money to spend. A number of tax and spending decisions will help close the budget gap for 2016 but will leave significant problems for the next governor and the fiscal 2017 budget.

Lawmakers have awakened to the expensive and unlimited tax credit programs that have grown sharply in recent years. PAR and some legislators for years have recommended a re-evaluation of the exemptions and credits that would weigh the interests of business, local governments and essential state services. These tax programs should be altered fairly and sensibly with a long-term restructuring. But lawmakers need fixes with short-term revenue gains to balance next year's budget, and so their solutions are following that lead. This PAR commentary highlights several key issues as the session nears the end on June 11.

Higher taxes in Louisiana

A package of tax changes in this session will increase the net tax burden on businesses and individuals. Examples include a new tax on cigarettes and other tobacco products, the suspension of a sales tax for business utilities and reductions in various exemptions. Many taxpayers receiving credits against taxes owed or paid will receive smaller credits. The exact overall impact depends on the final disposition of the bills and various assumptions and definitions used for calculations, but the increased burden is likely to exceed $700 million for next year, not counting "fee" increases.

Very large fee increases are in the works this session that would impact ordinary citizens as well as businesses. Among the biggest hits are increases in vehicle titles and driver's licenses. To the extent these increases exceed the true costs of the government service provided, they would actually be new taxes. At this point the new money is going into the state general fund and the Legislature intends to spend it on various government operating expenses.

The central package of revenue and spending bills does not offer anywhere near the level of tax decreases that would "offset" the tax increases to create a revenue neutral new tax environment. There is no revenue neutrality, as some might claim. The governor and some lawmakers view the SAVE bill, or Student Assessment for a Valuable Education, as an offsetting measure but that initiative is a Rube Goldberg budgetary contraption and not a tax reduction.

The SAVE initiative

The SAVE program would create a new obligation for state spending on colleges based on enrollment. Although it establishes a new assessment and tax credit, the program as currently conceived would not cost anyone any new fees or tuition and would not give anyone a real tax break. Its impact would be to guarantee a certain level of state funding to colleges on a per-student basis. Whereas the state's constitutionally created MFP process provides relatively stable state funding for local school districts, the SAVE program would use a different mechanism essentially to achieve a similar goal for higher education. It has won the strong support of higher education officials. An overall target figure of $350 million has been under discussion.

SAVE is a misuse of the tax system. The purpose of a tax system is to generate revenue to support needed public services. SAVE does not generate dollars for the state. Also, it does not promote any desired behavior such as a business tax incentive or credit might. It is being used merely to masquerade and promote tax increases.

The public should understand that SAVE does not provide any real reduction in taxes or fees and would not affect how much money the state has available to spend. It would reduce discretionary spending from the state general fund and obligate that spending to colleges. According to the governor's formula and toward his purpose of appearing not to raise taxes overall, the amount of SAVE spending would be counted numerically as an offset to proposed tax increases that have been moving through the legislative process this session.

SAVE is basically a vehicle to allow separate state tax and revenue increases with the governor's permission. It has become a critical piece of the budget puzzle this session only because of the governor's political priorities. The end result is that the governor, by his standards, pretends to keep his tax pledge, while the Legislature gets to spend the money. The governor is taking a political risk that he will be seen as an elected leader who raises taxes but will not take responsibility for it.

Another impact of SAVE is that it takes the state a further step backward toward enrollment-based funding for higher education. One of the better reforms made in Gov. Jindal's first term was to move the state's budgetary practice away from an enrollment-based approach and more toward performance-based funding. A growing consensus in Louisiana and nationwide was that enrollment-based funding has ill effects that drive quantity over quality. During the Jindal years, direct state funding of higher education diminished while colleges raised tuition substantially. Performance-based funding became less relevant than the reformers intended. This trend, when combined with the purely enrollment-based funding formula of SAVE, will mean that higher education in Louisiana will have firmly re-established student enrollment as its primary economic driver.

Problems and predictions

The state might face a large disparity between the budget passed this session and the real accounting of revenue and spending that takes place over the next fiscal year. PAR has previously identified a number of holes in the budget. Also, the estimates of savings from the various tax bills might be unreliable; the Legislative Fiscal Office says there are so many unknowns that it cannot be confident of its projections for some of the bills. And business decisions and practices will not remain static in the face of tax changes. Companies' behavior will adjust to fit the circumstances and to save money.

Some of the pieces of the budget puzzle involving lower exemptions and credits will create different standards for tax filers in the middle of the tax year. This situation will create serious problems, such as a double standard for taxpayers, possible legal challenges and state administrative costs. This element of the legislative proposals will contribute to the uncertainty about what the real impact on the state budget will be.

A number of elements in the evolving budget for fiscal 2016 will create a gap for next spring's fiscal 2017 budget challenge. For example, a business utility sales tax is being suspended for just over one year. Many reductions in tax exemptions and credits for fiscal 2016 would be recaptured by businesses in subsequent years. On the other hand, some tax changes would have no impact in fiscal 2016 but would boost state revenue or save money in later years.

Tobacco tax dedication

Lawmakers like to complain that the state budget process is too limited by dedications and yet they continually place more limits on themselves. The combined cigarette and tobacco taxes in House Bill 119 would raise an estimated $162.7 million per year. But the bill dedicates the revenue to a Medicaid match fund and then further limits the way money can be spent from the fund. These restrictions are unnecessary and counterproductive.

Medical schools

Louisiana's publicly supported medical schools have been among the lowest priorities in the state budget this year when they should be among the highest. House lawmakers made a contingency plan to finance them adequately but left the schools in serious jeopardy. The Senate version of the budget intends to take care of the schools.

Every spending program should be considered for cuts this year. The medical schools should face serious scrutiny about their spending practices. In this session, the potential deep cuts and uncertainties thrust upon the medical schools went far beyond efficiency measures and became a threat to the state's primary interests. Medical schools are critical to helping fill the vital healthcare positions needed in all areas of the state. The medical schools are fundamental components of economic and workforce development, community prosperity and citizen well being. The overall legal structure and priorities assigned in the state budget give higher preference to many other spending programs affecting the general fund, including local pork projects, private school subsidies and film credits, to name a few.

Film credits

The film credits program has been under scrutiny this session. While a bill by Rep. Joel Robideaux has attracted the most attention with its overall credit cap and other reforms, a separate bill by Rep. Katrina

Jackson would have a more profound impact on the program. Jackson's House Bill 629 would reduce a large variety of tax credits, including a change in the film tax credit program from a 30% compensatory credit to 24%. The bill is unclear about how and when the reduced credits would apply to the various stages of the film credit process.

Also, a suggestion was made in a committee hearing this session that the state should lower the state's automatic cash rebate for the film credits, which is currently at 85%. This cash rebate program has demonstrated a savings to the state of more than $50 million in the past five years. It should be kept at the same rate or, as discussed in a prior PAR report, be raised to 88%. Lowering the rebate rate to 75% or further would be a disincentive for movie makers to use the rebate and indeed would likely create a better cash flow for the state in the next fiscal year. But in the long run the state would be paying more. Lowering the rebate rate would be advantageous for tax credit brokers but would waste taxpayer dollars.

MFP spending

The Senate has taken the tough but right move by not granting an inflation increase in funding the Minimum Foundation Program, which distributes state money to local school districts according to a formula. The House had backed the plan by the state school board to increase the per-pupil state spending rate and lock the state into a higher annual minimum obligation. Although the state is required to spend more to accommodate growth in the student population, this year the House went further and added the inflationary increase, which is not required. That increase would have been locked into the state's future obligation for annual spending on local school districts.

The final puzzle

The next governor and Legislature elected this fall will find that a lot of pieces are missing from the state budget puzzle. They will have a lot of work to do to ensure that actions this session have not caused long-term damage to the state's business climate. As they repair the fiscal 2016 budget and plan for 2017 and beyond, they should consider certain types of spending cuts and budgetary and tax reforms suggested by PAR and other analysts of the state fiscal situation. A long-term restructuring should be led by the next governor, who should not expect to revamp everything successfully in the first few months in office. This job will be complicated by recurring budget shortfalls. But a new and more reliable plan for fiscal sustainability would be vital to the state government, the Legislature, businesses and the citizens of Louisiana.

For more information contact: Robert Travis Scott, President, 225-926-8414 ext. 221
robertscott@parlouisiana.org

P. O. Box 14776 Baton Rouge, LA 70898-4776 Phone: (225) 926-8414 Fax: (225) 926-8417
Web Site: www.parlouisiana.org