Taxes

Create a Fair and Competitive Tax Environment

Louisiana should provide a fair, simple and competitive tax environment for individuals and businesses that produces sufficient and stable revenue for essential government operations and services.

Taxes are only one piece of a state's economic and business environment, although an important one. Progress in education, poverty, workforce and infrastructure require planning and reinforcement over the long-term to achieve success, but tax problems are more readily within the grasp of legislators to change and improve. The biggest challenge is that a state's tax structure shapes an expectation about who should pay and also forms government dependence on particular revenue streams, thereby fostering a culture averse to change. In concept, a better tax code might appeal to the public and lawmakers. But in practice, tax changes, even if they create a better and more fair overall system, are likely to be felt unevenly among taxpayers and might distribute revenue differently for state and local agencies. Change is hard.

Louisiana is unusual in that its state rankings for average tax burdens on citizens and businesses tend to be close to the national average or even low, while its tax rates are relatively higher than most other states[i]. The rates are high but the actual average tax bill is often at or below average. That is a picture of a broken system. Some taxpayers are exposed to high rates and some are not. From an economic development standpoint, high rates are a disincentive to live, invest and hire workers in Louisiana. A system with high rates and low returns means Louisiana does not possess the traits of a good and competitive tax system – fairness, simplicity, transparency, neutrality and stability.

As a result of its system of tax incentives and exemptions combined with high rates, Louisiana's tax and business climate rankings on a national scale are a mixed bag of scores. Certain types of businesses and investments have an advantageous tax situation in Louisiana[ii]. For example, Louisiana has strong incentives for new corporate headquarters that could help offset a tax structure that otherwise is unfavorable to them, but this strategy has rarely made a difference. Many manufacturing operations enjoy one of the lowest income tax burdens in the country because of the way Louisiana taxes multi-state operations and maintains a low unemployment insurance tax burden. But these firms also face among the highest sales and property tax burdens in the country, due to taxes on equipment and other factors.

Louisiana has become a complicated bag of tricks, scoring well in some of Site Selection magazine's tax rankings and poorly in others, such as Forbes' "Best States for Business" which weighs numerous factors besides taxes. "Non-neutrality – across firms, maturity, and tax types – proves a central feature of the Louisiana tax code," according to the Tax Foundation, a major critic of the state's tax system.

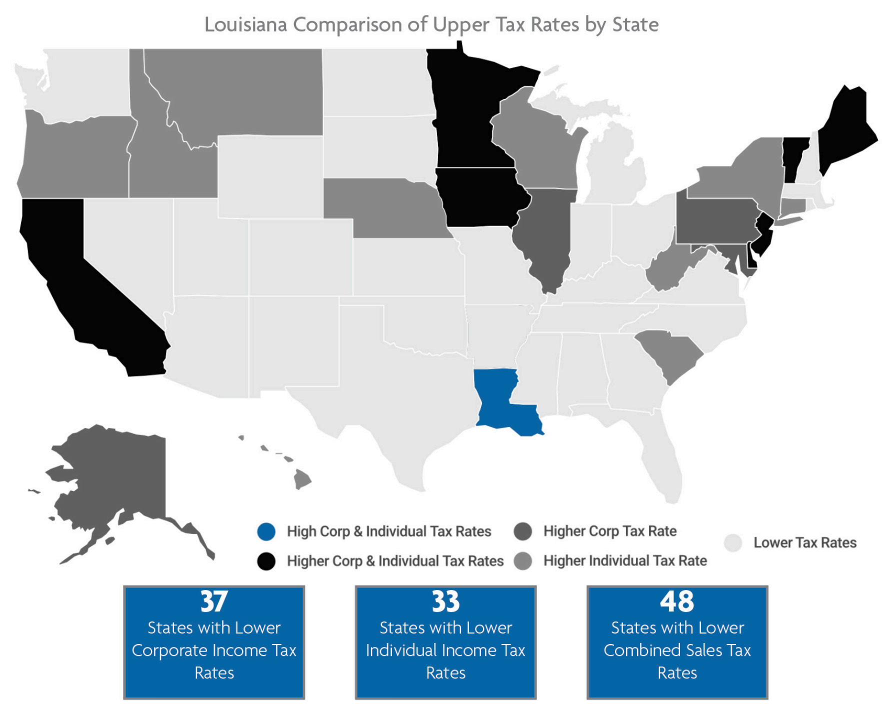
The top revenue sources for Louisiana are the sales tax and the individual income tax, followed by gambling taxes and insurance premium taxes. Mineral revenue has had decreasing impact over the years but can inflate with higher energy prices. With large credits and exemptions in place, corporate income and franchise taxes usually account for less than five percent of overall net state tax revenue[iii]. However, businesses pay far more than that to state and local governments, including: about half of all sales taxes, the majority of property taxes, revenue from businesses filing through the individual income tax, and many local and state regulatory and occupational licensing fees[iv].

At 9.45%, Louisiana has the second highest average combined state and local sales tax rate in the nation[v]. That is only a fraction below Tennessee, which has no income tax except for investments. The state has close to 200 sales tax exemptions, of which approximately 100 were suspended temporarily in 2018. Exceptions to the sales tax tend to narrow the base and place upward pressure on rates.

Louisiana is one of very few states where local governments collect the sales tax, a system that places businesses at a disadvantage because of multiple rates, a lack of uniformity, different rules interpretations and multiple audits.

High Income Tax Rates

Unlike the great majority of states, Louisiana allows a deduction for federal income taxes paid on individual and corporate income taxes. Eliminating that deduction, when accompanied by appropriate state tax rate reductions, would decouple Louisiana's income and corporate tax base from federal tax changes. Eliminating federal tax liability as a deduction for the income tax would break the connection between federal changes in tax policy and state income tax collections. The state should neither be rewarded when the federal government decides to lower taxes, nor penalized when they are raised. This approach would better align Louisiana with its competitor states, provide a more stable source of revenue than the current corporate income tax structure and eliminate instability in state corporate tax collections due to actions in Washington, D.C. After Arkansas lowers its rate as planned, only one other state in the Southeast will have a higher individual income tax rate than Louisiana's top rate of six percent. Thirty-three states have a lower top rate than Louisiana or no income tax[vi]. In some of these states, their top rate kicks in sooner on the income scale than in Louisiana, lessening the difference. But overall the higher rate makes our state look unattractive.



Louisiana's upper tax rate on corporate income of eight percent is high compared to other states in the South and Central regions of the country[vii]. The high rate creates a large tax liability that is diminished by tax credits, net operating loss offsets and exemptions. Even though the net amount of income tax paid by Louisiana corporations overall is in line with many other states, the higher absolute rate creates the strong perception, and for some companies the reality, of a barrier to economic development. Arkansas Governor Asa Hutchinson has taken advantage of Louisiana's tax weaknesses with a recently passed business tax bill that lowers rates. "It is a truly comprehensive, competitive tax bill that will put us in a better position with our surrounding states and support our industries and our businesses to a greater extent," Hutchinson said.

The franchise tax is a tax on wealth and investment that is widely recognized as a complex and antiquated type of taxation that discourages investment, inhibits economic development, provides a disincentive to corporate headquarters operations and causes costly compliance and auditing problems. Audits and lawsuits are more common with the franchise tax than with income taxes. Only 13 other states have a corporate franchise tax, most at token levels of taxation, and only one other has a rate higher than Louisiana. Two of those states – including Mississippi – are phasing out franchise taxes. Five other states recently phased out theirs[viii].

It is long past time that Louisiana restructure, phase out or eliminate the corporate franchise tax. If the state wishes to identify replacement revenue that coincides with lower franchise taxes, it may look to the corporate income tax, certain tax credits and utility bill sales taxes as potential trade-offs. Alternatively, the state could create a raised floor for the taxable base for the franchise tax, with companies below the floor free from the tax. Raising the floor of the taxable base would relieve the regulatory problems and litigation expenses for the majority of companies filing the franchise tax, as well as relieve the state revenue department's burden of regulation and litigation, with minimal revenue impact to the state.

For the Industrial Tax Exemption Program (ITEP), decision-makers should weigh the overall tax environment, the manufacturer's return on investment for capital expenditures, the predictability and stability of the incentive program and the overall competitive nature of the deal versus other states. The impact on Louisiana service and vendor contractors supporting manufacturing improvements must be weighed into decisions, as these are major ongoing employment and commerce factors in Louisiana.

Capital investments should be encouraged, even when they do not produce large numbers of direct jobs. The great majority of states do not tax capital manufacturing investments as heavily as standard expenditures, such as for sales taxes and property taxes. Louisiana should limit the number of local entities involved in granting the exemption in a way that is competitive with other states in the Southeast.

Local Taxes

Property taxes are a local revenue source set at relatively low rates and carry a low tax burden in Louisiana, with significant exemptions. The property tax is one of the reasons Louisiana ranks high in Kiplinger's list of "tax friendly" states, which emphasizes retirement considerations. Others see the situation differently and point out that Florida and Texas, with no income tax, have seen large in-migrations from other states despite high property taxes.

In Louisiana, a large homestead exemption, an assessment freeze for the elderly and additional breaks all add up to a relatively meek property tax revenue stream. For example, in Louisiana, property taxes support public schools at half the level as the average among other states[ix]. Half of the state's parishes have 49% or more of their homesteads 100% exempted. Fully exempted homesteads account for just over a third of all homesteads statewide. The freeze on assessments for those individuals 65 and older is in place for about one of every 15 homes[x].

Local governments are far more dependent on the sales tax, which is more volatile than the property tax. In some rural parishes, the proportion of totally exempted homes is vast and the retail sales are scarce. One long-term way to address these problems would be to lower the sales tax or the individual income tax while raising property tax revenue for local governments, and then decrease some state spending allocated to the local governments. This strategy would be a difficult but potentially beneficial reform that would create a tax system more similar to the economically successful states that Louisiana might wish to emulate.

The RESET

- **Louisiana should adopt a better tax system. It is not about increasing or decreasing taxes, it is about how the state collects taxes. Louisiana should continue to expand the sales tax base and reduce the sales tax rate, including the taxation of some services, such as those taxed in Texas.**
- **Louisiana should permanently suspend the 100 sales tax exemptions the Legislature has temporarily suspended.**
- **Louisiana should implement a more uniform and centralized system of sales tax administration, collection and audit that respects and protects local revenue streams and businesses. Collection of tax from Online and shipped sales should be consistent with federal law and court rulings.**
- **Louisiana should eliminate the deduction for federal income taxes paid on individual and corporate income taxes – accompanied by appropriate state tax rate reductions.**
- **Louisiana should phase out, eliminate or restructure the corporate franchise tax.**
- **Louisiana should weigh the overall tax environment, the manufacturer's return on investment for capital expenditures, predictability and stability, the broader regional job impact and the overall competitive nature of the Industrial Tax Exemption Program (ITEP).**
- **Louisiana should expand the use of Payment-In-Lieu of Tax arrangements for local governments considering property tax exemptions to attract economic development.**
- **Louisiana should consider lowering sales tax or the individual income tax rates while raising property tax revenue for local governments, and then decreasing some state spending allocated to the local governments.**

Endnotes

i The Tax Foundation

ii The Tax Foundation, "Location Matters." For example, the Forbes "Best States for Business" ranking puts Louisiana at No. 42 although the state's tax ranking portion of that survey, drawn from the Tax Foundation, is more favorable to the state.

iii Louisiana Department of Revenue annual reports

iv James Richardson, et al. "Exploring Long-Term Solutions to Louisiana's Tax System" and The Council on State Taxation.

v The Tax Foundation

vi The Tax Foundation

vii The Tax Foundation

viii The Tax Foundation and PAR research

ix National Center for Education Statistics, "Public School revenue Sources."

x Louisiana Tax Commission Annual report 2018