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RESET Tax Study Highlights

Overview

RESET Louisiana is a nonpartisan collaboration between the Council for A Better Louisiana, the Public Affairs Research Council of Louisiana and the Committee of 100 for Economic Development. Its goal is to pursue public policy initiatives that will improve the state's future.

As part of this work, RESET hired well-known economist and fiscal expert Greg Albrecht to conduct an independent analysis of the tax reform plan recently proposed by Gov. Jeff Landry's administration for debate during an upcoming special session of the Legislature. The intent of this study is twofold: 1) to provide an independent review of revenue estimates to determine the impact of proposed income and sales tax changes on Louisiana citizens across a wide spectrum of income levels, and 2) to evaluate the reasonableness of certain of the revenue estimates provided by the Louisiana Department of Revenue.

Albrecht has a wealth of experience in performing this type of analysis. He worked at the Louisiana Legislative Fiscal Office from 1985 until 2022, serving as the office's chief economist from 1991 until his retirement from state government. In that role, Albrecht tracked economic trends and tax collections, analyzed the potential financial impacts of proposed legislation and devised income forecasts from which lawmakers built the state budget. He currently serves as a research fellow at the LSU Center for Energy Studies, where he helps estimate the financial impacts of energy investments.

In this study, Albrecht has modeled the potential tax liability impacts of the Landry administration's proposed personal income and sales tax changes on households at various income levels. The study looks first at the income tax, then the sales tax and then analyzes what the combined tax changes could mean for taxpayers across a wide range of income brackets.

This is important because income and sales taxes are the primary taxes that individuals and families pay to the state. When combined, they make up close to 60% of state government's current tax collections. This study does not assess the potential impact of other components of the package.

RESET supports the broad concepts of the governor's tax reform plan to simplify and modernize Louisiana's uncompetitive tax system. But we also believe an independent review of what those changes mean for taxpayers is key to helping legislators and the public consider and understand the ideas that are being proposed.

Methodology

AS WITH ALL REVENUE ESTIMATION MODELS, THE METHOD USED TO FORECAST THE IMPACT OF THE ADMINISTRATION'S PROPOSALS BY INCOME RELIES ON A NUMBER OF ASSUMPTIONS. THE SALES TAX IMPACT IS EVEN MORE DIFFICULT AS IT REQUIRES ASSUMPTIONS ABOUT HUMAN CONSUMPTION, WHICH MUST BE TRANSLATED INTO TAX REVENUE ESTIMATES. THE FULL REPORT WITH ALL DETAILS, DISTRIBUTION TABLES, ASSUMPTIONS AND DATA SOURCES CAN BE FOUND AT HTTPS://WWW.RESET-LOUISIANA.COM/STATEFINANCES

Summary of Findings

Purpose

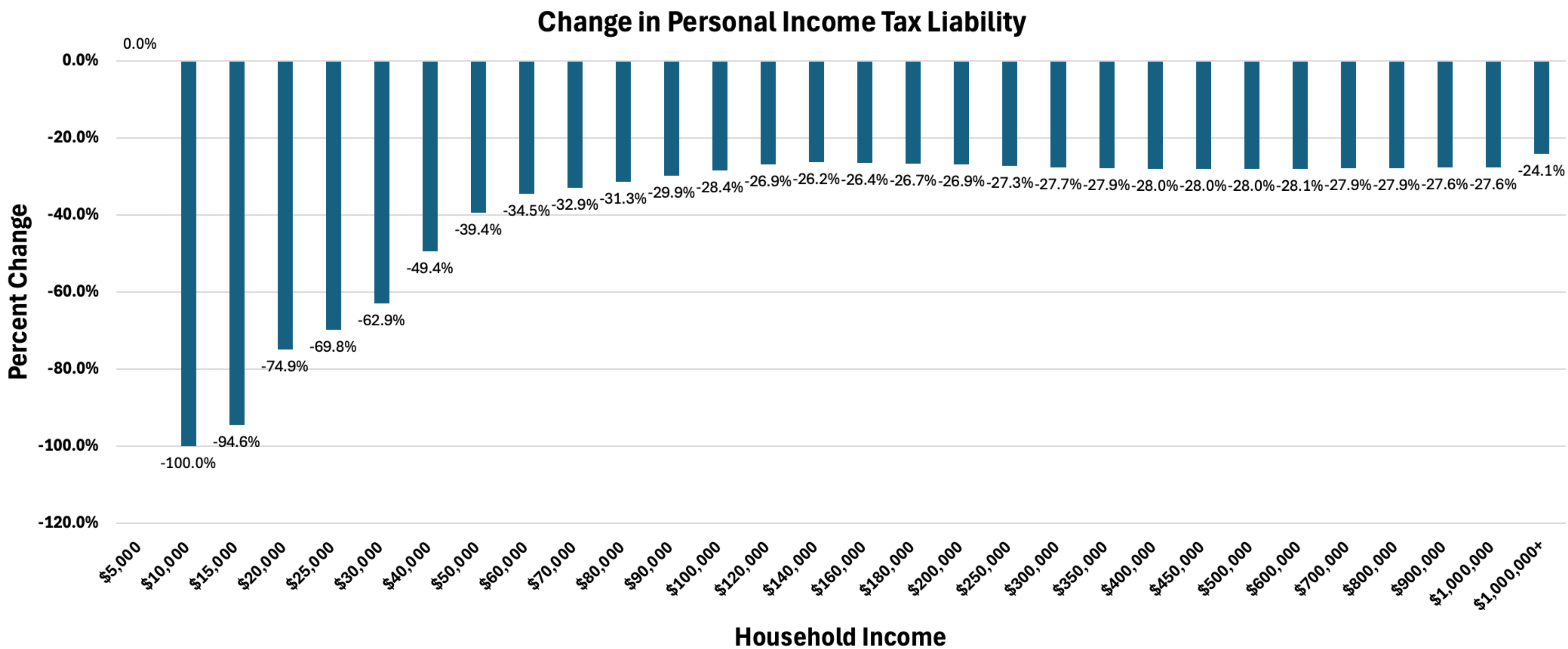
This study evaluates the changes the Landry administration has proposed to state income and sales taxes. It utilizes income tax data from more than 1.7 million actual Louisiana income tax returns and sales tax collection modeling from the Louisiana Department of Revenue to estimate the impacts of the tax proposals on taxpayers across 30 income brackets. It also provides an independent set of revenue estimates that allows citizens to compare these projections to those generated by the Louisiana Department of Revenue.

Proposed Income Tax Changes

- The administration's proposal applies a single 3% tax rate to all taxable income. Overall, this results in a lower marginal tax rate for the middle and top tiers of taxpayers who are now paying 3.5% and 4.25%, respectively.
- Further, it basically reduces taxable income for all taxpayers by increasing the standard deduction. In doing so, it effectively eliminates the tax entirely for the current bottom tier of tax filers who are taxed at a rate of 1.85%.
- Deductions of $1,000 for dependents, retirees over age 65, and the blind are eliminated, but the loss of these deductions is more than offset by the other income tax changes.
- The elimination of deductions for business capital gains and Internal Revenue Code 280C expenses (dealing with certain business deductions and credits) tend to impact only taxpayers at upper income levels and with only a minimal effect on their tax liabilities.
- While the dollar amount of tax reductions gets larger as income rises, the percentage of the reduction in tax liability tends to be larger at lower incomes. In that sense, the proposed income tax changes appear to increase the progressivity of the state income tax compared to the current system.
- However, about 54% of the total income tax reduction will go to the top 10% of income filers – those with adjusted gross incomes of $150,000 or more. About 46% of the cut will go to the remaining 90% of households reporting lower incomes. This is largely a function of the fact that those at higher incomes generally pay a larger dollar amount of income taxes.
- In Louisiana, income for most businesses is taxed through the individual income tax not the corporate income tax. Because of this, the income tax reductions shown in the study's tables are effectively reducing income tax liability not only for individuals and households, but also for businesses in the state.
- The report notes, however, that the inclusion of business taxes in the individual income tax tends to distort the impacts seen in the tax tables for filers reporting very low levels of adjusted gross income. This is because a significant number of those returns show a pass through of business income losses.
- The Louisiana Department of Revenue income tax estimates are very close to the projections generated by the RESET simulation model. The state estimate of the overall income tax cut is only 1.15% higher than the RESET independent model.
- However, the LDR estimates do not appear to take into account nonresident and fiduciary filers. When those are included in the model, the overall reduction in individual income tax revenues increases by $45 million.

Income Tax Changes by Household Income Level

The graph below shows the impact of the tax cut by income level. This includes all statutory proposed changes to the income tax. Those at lower income levels receive the largest percentage of tax reduction and make up the largest number of taxpayers. As an example of the impact, there are 183,891 households reporting an adjusted gross income between $30,000 and $40,000. They represent the largest number of taxpayers in any single bracket. They would receive a nearly 50% income tax decrease, or $338. By comparison, those making $600,000 to $700,000 would receive a 28% tax cut worth slightly over $7,000. However, that would only affect just over 3,000 households. This proposal can be seen as modestly progressive since lower-income households receive a higher proportional cut.



Proposed Sales Tax Changes

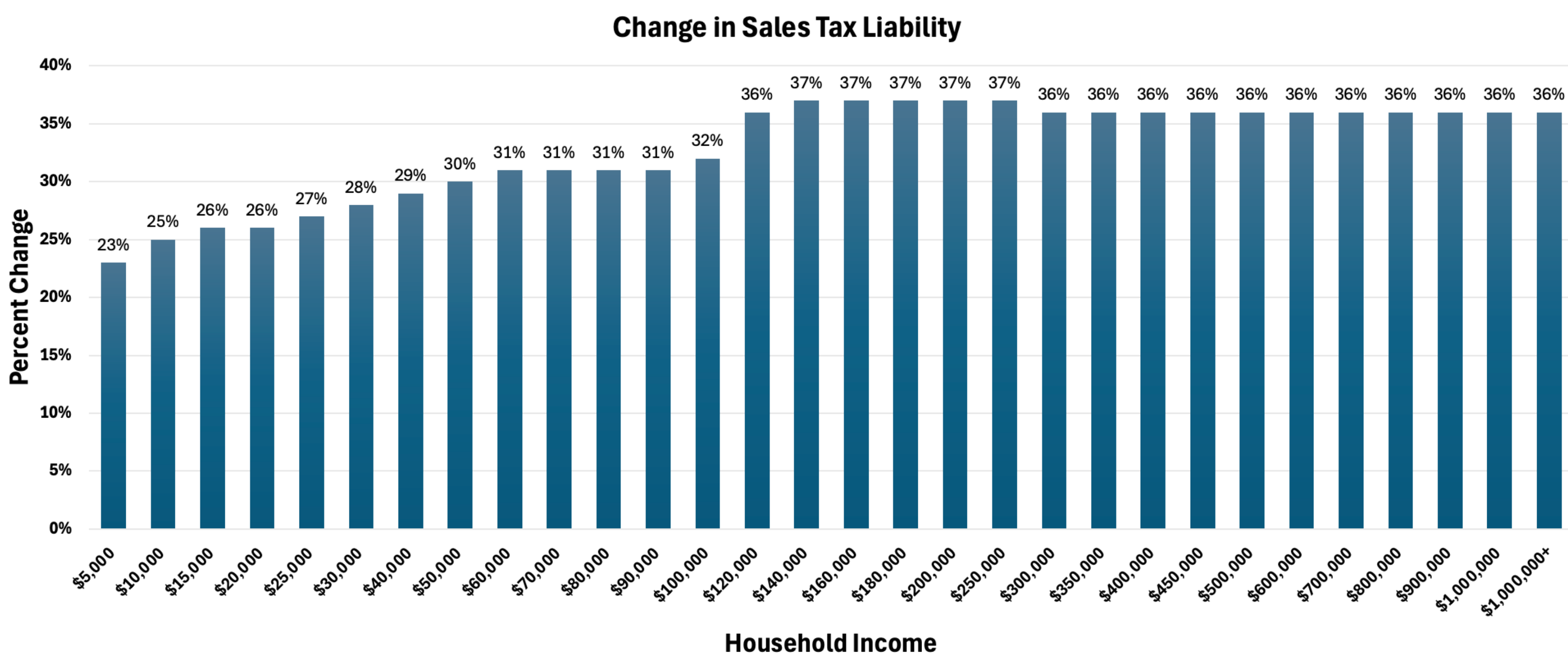
- All resident households are likely to see an increase in their state sales tax liability as a result of the proposal to apply sales taxes to digital goods and other services and transactions.
- Both the percentage of liability and the absolute dollar amount of the tax increase gets larger as income rises. Thus, the proposed changes in sales tax appear to slightly reduce the overall regressivity of the state sales tax as compared to the current system.

- The study notes that the top 10% of taxpayers in the state will pay about 37% of the total sales tax increase with 63% being borne by the 90% of taxpayers with lower incomes. This is because, in general, those with higher incomes spend higher amounts of money and thus pay higher amounts of sales tax.
- The model further estimates that it seems likely that Louisiana households will be responsible for less than half the increase in sales tax collections, with the rest of the liability paid by others such as nonresidents, tourists and businesses.

Sales Tax Changes by Household Income Level

This graph demonstrates the effect of the sales tax change by income level. It only includes households, not the impact on businesses. It shows that filers at lower income levels will see a smaller percentage increase in their sales tax liability than those at higher income levels.

Looking at the same taxpayers as in the graph above, those households in the $30-$40,000 range would pay 29% more in sales taxes annually with an estimated cost of $96. By comparison, those making $600-$700,000 would pay 36% more in sales taxes or $826 on average each year. This proposal can be seen as modestly less regressive than the current sales tax system since higher-income households receive a higher proportional increase.

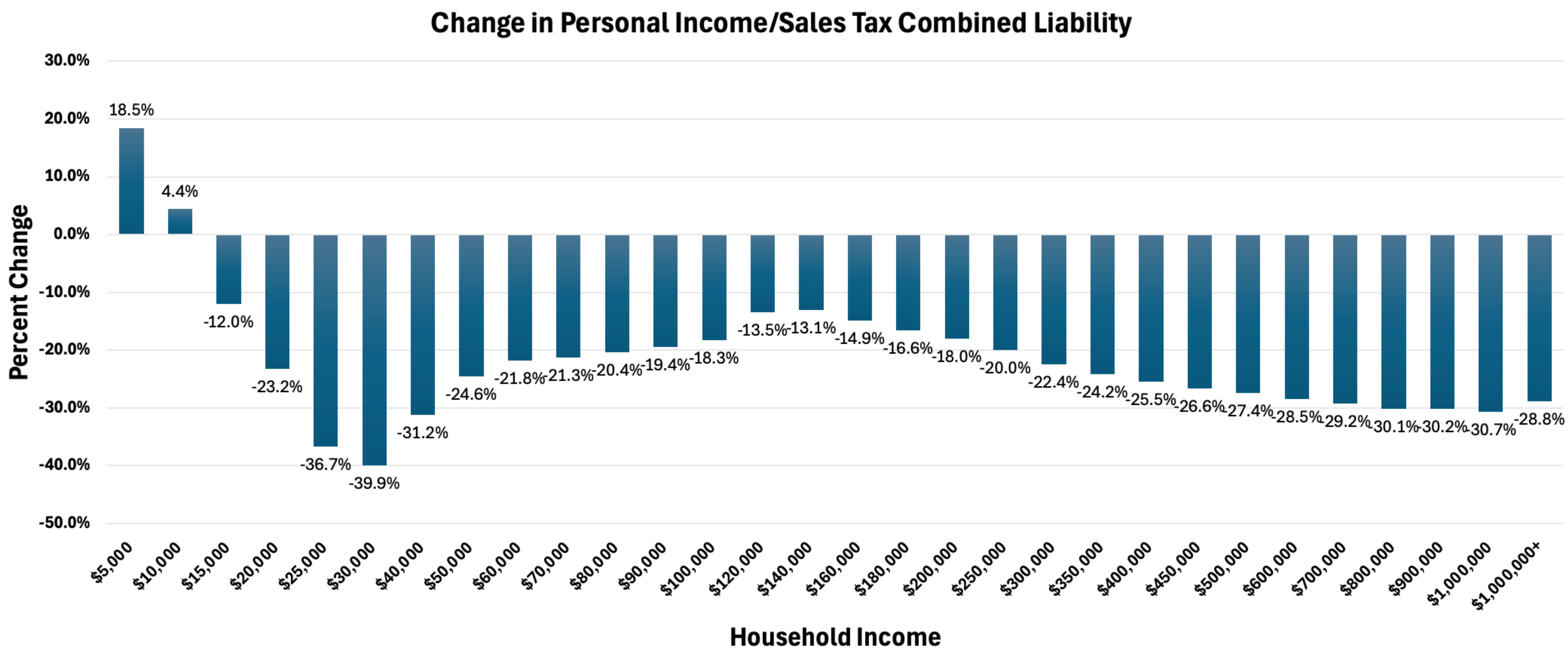


Impact of Combined Income and Sales Tax Changes

- When looking at the combined impact of the changes to the individual income tax and the state sales tax, most resident households are likely to see a reduction in their overall tax liability. That is because the reductions in income taxes are generally larger than the increases in sales tax.
- The study also shows that overall, the proposed changes to income and sales tax make only slight changes to the way the liability of those taxes is distributed under the current system.
- Under the new plan, about 1,078,000 households would receive a reduction of 20% or more in their combined sales and income tax liability. Of those taxpayers, 91% have adjusted gross incomes between $15,000 and $80,000.
- Those between $80,000 and $250,000 would still see a net reduction in income and sales taxes, but in a range from about 13% to 19%. Those with incomes above $200,000 would also see tax reductions of 20% or more, but they represent fewer than 100,000 taxpayers.
- There are about 151,000 households with reported incomes between $0 and $10,000 who would see a slight increase in their taxes. As noted before, this includes households that report significant amounts of gross income, but also report large business losses that are carried over to their individual income tax returns.
- In other cases, this group includes taxpayers who were likely paying little to no income taxes to begin with. Because of this, they were unable to realize any meaningful benefit from the across-the-board reduction in personal income taxes, though they were still impacted by the increases in the sales tax. Nonetheless, the estimated tax increase for these households is extremely small, averaging between $9 and $29 per year.

Combined Income and Sales Tax Changes by Income Level

The graph below shows the combined effects of the proposed individual income and sales tax changes by household income level. The two lowest income categories (between $0-$5,000 and $5,000-$10,000) would see an increase in annual tax payments. The increase would be 18.5% for those $0-$5,000 (or $29 annually) and a 4.4% increase for those between $5,000-$10,000 ($9 annually). This is because these groups currently pay little to no income tax but would pay more in sales tax. By contrast, the largest cuts go to households who make $25-$30,000 with an almost 40% reduction in combined sales and income taxes ($224 annually).


Change in Personal Income/Sales Tax Combined Liability
30.0%
20.0%
10.0%
0.0%
-10.0%
-20.0%
-30.0%
-40.0%
-50.0%
Percent Change
18.5%
4.4%
-12.0%
-23.2%
-36.7%
-39.9%
-31.2%
-24.6%
-21.8%
-21.3%
-20.4%
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$100,000
$120,000
$140,000
$160,000
$180,000
$200,000
$250,000
$300,000
$350,000
$400,000
$450,000
$500,000
$600,000
$700,000
$800,000
$900,000
$1,000,000
$1,000,000+
Household Income

Conclusion

The primary focus of the RESET study was to provide information about the impacts of the proposed changes to state income and sales taxes on taxpayers across a wide range of incomes. It also provides citizens and policymakers independent revenue estimates which they can compare to those generated by the Louisiana Department of Revenue.

In doing so, three major findings emerge:

1. In considering the changes to income and sales taxes, the vast majority of Louisiana citizens will see a tax cut, almost all in double digit percentages and more than half totaling 20% or more.
2. It appears that the income tax becomes modestly more progressive, and the sales tax becomes slightly less regressive as a result of the proposed changes. Overall, the distribution of tax liabilities across all levels of income amounts to little or no change from the current system.
3. Revenue estimates of individual income tax impacts between the Louisiana Department of Revenue and the independent RESET model are very close. However, LDR should update their estimates to account for nonresident and fiduciary filers, as noted earlier.

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