PAR LOUISIANA | COMMENTARY

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Overhauling Louisiana's Tax Structure

Governor wins support for most of his tax reform ideas, but lawmakers stall some plans

Louisiana lawmakers embraced much of the tax rewrite package sought by Gov. Jeff Landry in the just-ended special session, agreeing to lower and flatten income tax rates in exchange for new sales tax charges.

Across the two-week session, the House and Senate largely supported the tax swap effort, but they balked at Landry's efforts to broaden sales tax to cover new services and protected several tax break programs the governor sought to scrap. Lawmakers also jettisoned proposals to eliminate taxes at the local level that aren't charged by the state.

Still, Landry won more than he lost in the pre-Thanksgiving session.

Lawmakers cut income tax rates for people and businesses, repealed a corporate franchise tax that few states have and removed a number of tax breaks across tax types.

They agreed to a sweeping rewrite of the budget and tax section of the Louisiana Constitution that – if approved by voters in March – will pay down retirement debt, merge state savings accounts and help provide money for a permanent teacher pay raise rather than one-time stipends.

And they appear to have largely solved a looming fiscal cliff that had threatened to force significant cuts to programs and services.

The Public Affairs Research Council of Louisiana sees much to applaud in the work done. Landry and lawmakers started simplifying Louisiana's messy and complicated tax structure, ended a noncompetitive corporate franchise tax, steered billions of dollars to retirement debt payments, removed some unnecessary clutter from the constitution and hopefully ended an immediate budget crisis.

But in PAR's opinion, the Legislature made – and Landry agreed to – some missteps. They again used temporary budget and tax maneuvers that could create problems for long-term fiscal stability. They enacted new, unnecessary budgeting restraints that could make financial decisions more complicated in the future. And they missed an opportunity to bolster the state's "rainy day" fund and hedge against overreliance on volatile revenue sources for ongoing expenses.

Starting Jan. 1, Louisiana will have a flat 3% individual income tax rate and 5.5% corporate income tax rate. But rather than newly charge sales taxes across dozens of service types, the House and

Senate instead bumped up the sales tax rate to 5% through 2029, in a state that already has the highest average state and local sales tax rate in the country.

The bottom line effect of the total tax package on the state budget and taxpayers isn't yet entirely clear.

Lawmakers seemed confident the package of a dozen bills would close most, if not all, of a budget gap on the horizon for the upcoming financial year that begins July 1. The state's income forecasting panel, the Revenue Estimating Conference, will determine the true impact as early as December.

A last-minute flurry of changes made to the bills in the Senate made it difficult to immediately determine how the tax swap will play out for taxpayers.

Certainly, those people and businesses who pay individual income taxes will see a tax cut, with the more significant cut for higher earners who paid a greater share of their income in taxes. However, it's unclear how the sales tax hike will offset the gains from the income tax reduction. It's possible lower-income earners may see most, if not all, of the money gained from the income tax cut paid out on the increased sales taxes.

On the corporate tax side, most businesses will see a tax cut, but those who received specialized tax credits, exemptions or deductions and will lose them may not see as much relief as others.

Personal Income and Sales Taxes

Louisiana currently charges a graduated system of individual income tax rates that range from 1.85% for the lowest level of taxable income to 4.25% for higher income levels. That will become a flat 3% rate across all income levels in 2025.

With a flat rate, Louisiana will join a dozen other states that have a flat income tax, rather than tiered rates, according to the Tax Foundation, which tracks tax issues across states. Seven states don't charge income taxes.

Individual Income Tax Rates
(for single or married filing separately)

Taxable Income	Current	Starting Jan. 1
$0 - $12,500	1.85%	3%
$12,500 - $50,000	3.5%	3%
$50,000 +	4.25%	3%
Standard deduction	$4,500	$12,500
Annual retirement income exempt from tax	$6,000	$12,000

Louisiana's top rate of 4.25% was already lower than 35 of the 41 states that levy a personal income tax on wages and salaries, including all states in the Southeast that charge an income tax. With the new 3% rate, only two states (Arizona and North Dakota) will have a lower individual income tax rate, according to the latest Tax Foundation data.

To ensure the change doesn't raise taxes on low- to moderate-income earners, Landry and lawmakers will nearly triple the standard deduction from $4,500 to $12,500 for those who file as single or married filing separately. In other words, the first $12,500 of income won't be taxable at all. The amount doubles to $25,000 for those who file as married filing jointly, qualified surviving spouse or head of household. The deduction will grow annually by an inflation factor.

In addition, the tax exemption for pension and annuity income received by anyone 65 years old or older will grow larger next year. Currently, $6,000 of that annual retirement income is exempt from income tax. That will double to $12,000, and the exemption will be adjusted yearly for inflation, giving retirees a significant tax cut.

The income tax cut is estimated to cost the state treasury more than $1.1 billion in lost revenue it would have otherwise collected in the budget year that starts July 1 and more than $1.3 billion a year later, according to the nonpartisan Legislative Fiscal Office.

Lawmakers removed triggers in law that allowed for future income tax cuts if certain revenue benchmarks were hit. They'll have to vote if they want to cut tax rates further.

To offset much of the revenue loss and continue paying for ongoing programs, Louisiana's state sales tax rate will grow to 5% in the new year, up from a current 4.45% rate. That 5% sales tax rate will remain in place through 2029 and then fall to 4.75% in 2030.

Louisiana has had a seven-year, temporary state sales tax of 0.45% on the books that was set to expire in mid-2025. At that time, the state sales tax rate would have fallen to 4%. The extra 1% tax hike – which equates to an extra penny paid in tax on every dollar of sales – will raise an estimated $1.1 billion a year, according to the Legislative Fiscal Office. That's money that will help pay for the income tax cut.

State Sales Tax Rate

- Current
  4.45%
- Starting Jan. 1, 2025
  5%
- Starting Jan. 1, 2030
  4.75%

Landry didn't seek a 5% sales tax. He sought to keep the 4.45% rate and charge it across a new array of services, such as landscaping, home repair services, dog grooming, spa services, car washes, lobbying, personal training and more. But the House balked at the list and stalled the bill, so senators raised the tax rate and cherrypicked a few services, such as cable and satellite services, for sales tax charges instead. The House went along.

Lawmakers did agree to the governor's proposal to newly charge state and local sales taxes on some digital items, such as streaming services, audiobooks, online games and cellphone apps.

Local governments also charge sales taxes on top of the state rate. At the current 4.45% rate, Louisiana had the largest average local and state sales tax rate in the nation with a combined rate of 9.56%, according to the Tax Foundation. That will only grow larger.

To fill in budget gaps, the Senate decided to temporarily divert at least $280 million in sales taxes charged on vehicle purchases that were slated to pay for road and bridge work and to flow into dedicated funds for construction on Interstate 49 North and South and a new bridge in the Baton Rouge region. The House agreed to the Senate's plan to allow those vehicle sales tax dollars to pour into the state general fund for two years instead, where they can be spent on ongoing government expenses rather than transportation projects.

Left on the cutting room floor was Landry's attempt to prohibit local governments from charging sales taxes on prescription drugs. The state doesn't charge sales tax on medications. The local sales tax raises an estimated $250 million for parishes and municipalities, and efforts to backfill the lost local tax revenue fell apart.

Business Taxes

Most businesses tend to pay their taxes through the personal income tax system, so they will see the same tax cuts as individuals. Larger businesses who pay through the corporate income and franchise tax system also will see their rates drop.

Louisiana currently charges a graduated system of corporate income tax rates that range from 3.5% for the lowest level of taxable income to 7.5% for higher income levels. That will become a flat 5.5% rate across all income levels in 2025. To ensure the change doesn't result in any tax hikes for corporations, lawmakers created a new standard deduction for the first $20,000 of taxable income.

Corporate Income Tax Rates

Taxable Income	Current	Starting Jan. 1
$0 - $50,000	3.5%	5.5%
$50,000 – $150,000	5.5%	5.5%
$150,000 +	7.5%	5.5%
New standard deduction		$20,000

Of the 44 states that have a corporate income tax, Louisiana's upper rate of 7.5% ranked 14th-highest in the country and above other states in the South, though the effective rate was lessened by an array of tax breaks offered to businesses. The reduction to 5.5% will drop Louisiana below the top tier rates of at least 30 states, according to the latest available Tax Foundation data. In the South, Louisiana will maintain a higher corporate income tax rate than many of its peer states, including Mississippi and Arkansas.

Landry and lawmakers also repealed the corporate franchise tax for larger businesses (the tax already wasn't charged for small businesses), a tax that many states don't have and that is considered an impediment to business investment and economic development.

They continued a 2% state sales tax on business utilities that raises an estimated $230 million per year and had been scheduled to expire in mid-2025, and they did away with or capped a number of business tax break programs.

Louisiana's spending on film tax credits will shrink to $125 million a year (down from $180 million). A new cap will limit spending on tax credits for the rehabilitation of historic buildings to $85 million annually and on the research and development tax credit program to $12 million yearly.

No changes were made to the severance tax rates charged on the oil and gas industry, despite proposals from Landry to rework the structure. Also scrapped was an attempt to eliminate local taxes charged on manufacturing machinery and equipment.

Lawmakers did try to move parish governments away from charging property taxes on business inventory, a tax not charged by many other states. Currently, the state gives businesses a partial tax credit for the inventory taxes they pay to local governments.

The state will offer parishes a one-time payment up to $15 million if the sheriff, school board and parish governing authority decide to stop charging the inventory tax by July 2026. If a parish chooses to phase out the inventory tax over a five-year span, the state will offer parishes a one-time payment up to $10 million. The one-time sweetener will seek to replace three years of average inventory tax collections.

Additionally, a parish could allow a partial exemption of the inventory tax to businesses by reducing the assessed value of the property.

But the inventory tax changes only take effect if voters agree to a constitutional change in March.

Whether or not voters approve the other inventory tax changes, the state-issued credit for inventory taxes paid will end for corporations defined as a C corporations under federal rules, starting in July 2026.

Constitutional Rewrite

As part of the tax work, the Legislature also agreed to a hefty overhaul of Article VII of the Louisiana Constitution, dealing with revenue collection and taxes. The changes cannot take effect unless voters approve a constitutional amendment in a special statewide election to be held March 29 at a cost of $3.3 million.

PAR, as always, will write a comprehensive guide to the constitutional amendment ahead of the election. At a high level, the proposed changes would:

- Use nearly $2 billion stored in education trust funds to pay down retirement debt, lessening the cost of retirement payments for K-12 public school systems and for public colleges by an estimated $283 million a year and saving more than $1 billion in interest payments.
- Require public school systems to use their retirement payment savings to provide a $2,000 permanent teacher pay raise and $1,000 school support worker pay raise. Teachers and support workers have received those payments for the last two years as one-time stipends that weren't guaranteed to reappear year after year.
- Enact new limits on annual growth in state general fund spending on ongoing programs and services starting in the 2026-27 budget year, with the limit tied to state population changes and inflationary factors. Lawmakers could spend money above the limit but only on one-time items that don't grow ongoing expenses.
- Require a two-thirds vote for lawmakers to enact new tax break programs.
- Merge two state trust funds, the Budget Stabilization Fund (commonly known as the state's "rainy day" fund) and the Revenue Stabilization Trust Fund. The Budget Stabilization Fund would grow to about $2.8 billion and reach its cap so that no new deposits likely would be added for several years, at a minimum. The Revenue Stabilization Trust Fund would eventually disappear. New dollars that otherwise would have flowed into the Revenue Stabilization Trust Fund instead would be diverted into the state general fund and available to lawmakers for spending with few restrictions, possibly giving lawmakers hundreds of millions of additional dollars for spending.

One of PAR's biggest disappointments from the special session involved changes the Senate made to the consolidation of the trust funds.

While the Budget Stabilization Fund would be larger, and the dollars would have stronger protections from legislative raids, senators removed language proposed by Landry and sought by PAR that would have allowed for future deposits of corporate and severance tax collections.

Those two tax types are highly volatile and have fluctuated widely over the years – raising concerns about budget stability.

The Revenue Stabilization Trust Fund provided protections against an over-reliance of the two tax types for state operating expenses by requiring some of the money to be diverted to the savings account. The Landry administration proposed an approach that would have continued to hedge against the volatility by sending a percentage of the money to the rainy day fund or requiring its use on one-time items rather than ongoing programs and services.

But senators removed that language, and the House agreed to the change. Senate leaders have pledged to discuss potential adjustments to the rainy day fund language in the 2025 regular session. Based on those assurances, PAR is hopeful the conversations will continue.

The true implications of the sweeping changes enacted by lawmakers won't be known for months, if not years. The state's economists will tweak the forecasts as best they can to account for the tax overhaul, and the governor will build his budget proposal early next year off those forecasts, which are certain to need adjustment over time.