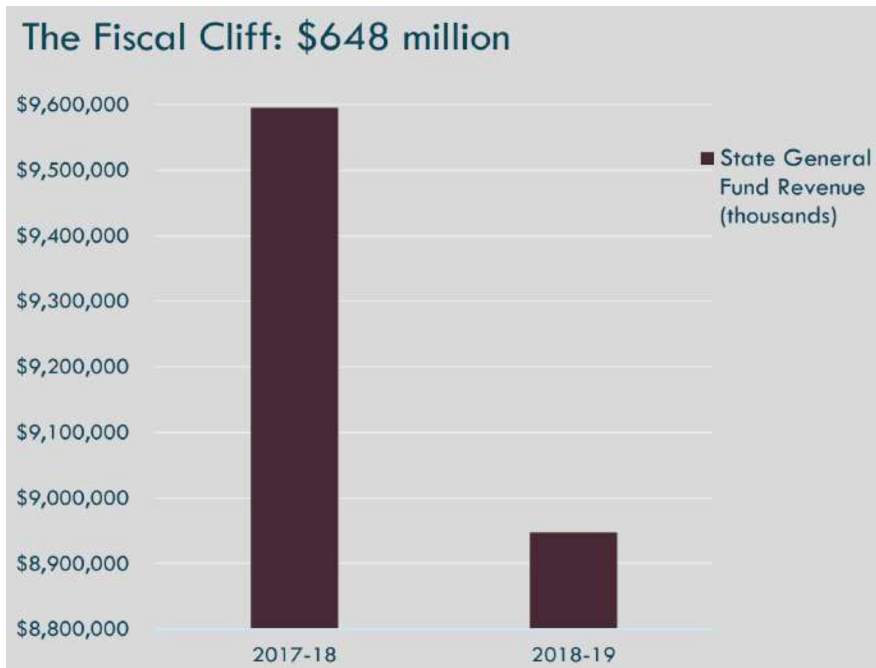
Louisiana Budget Project

Louisiana's Fiscal Cliff: The Basics

The Legislature will reconvene May 22 through June 4 for a special session focused on raising or retaining enough revenue to craft the 2018-19 state budget without damaging cuts to higher education, health care and public safety services. The special session is necessary because $1.4 billion in revenue that supports this year's budget budget is expiring on June 30.

Louisiana's economy is improving, and so are tax collections. The federal tax-cut law that passed in December added more than $300 million to the state's revenue forecast because Louisianans will not have as much federal taxes to deduct on their state income tax returns. Thus, the difference between the state general fund in the current-year budget, and the revenue available for appropriation in the 2018-19 budget cycle, is $648 million. Failure to reach that revenue target in the special session will likely force cuts to health care, higher education and other programs.



Cuts to state government programs and services would not only impact the people who benefit from them, but would also have ripple effects throughout the state's economy in the form of lost jobs and decreased economic activity.

Any solution to the fiscal cliff needs to meet two critical tests: Adequacy and fairness. That means the Legislature needs to retain enough revenue to avoid cuts to critical services that have already been severely reduced over the past decade. And the tax changes should protect low-income families by ensuring they do not bear a disproportionate share of the cost.

Background

Louisiana's current budget problems are rooted in income-tax cuts approved in 2007 and 2008, when the state's economy was benefiting from record energy prices and a flurry of post-hurricane reconstruction activity. The tax cuts took around $800 million per year from the state tax base and gave rise to a period when state government became increasingly reliant on non-recurring revenue sources.

But in 2015 and 2016, as Louisiana faced a recession caused by a drop in energy prices, the Legislature agreed to raise revenue as an alternative to deep cuts to state services. Some of those increases were permanent, such as an increase in the tobacco tax and an insurance premium tax that is helping to finance the state's share of the cost of expanding Medicaid. But the biggest revenue-raising measure was a 1 percentage-point increase in the state sales tax, from 4 percent to 5 percent, which expires on June 30.

This temporary sales tax is often called the "clean penny" because it does not include many of the exemptions that apply to the rest of the state's 4 percent sales tax. It currently raises around $880 million per year. While the Legislature has several options for raising the $648 million needed to maintain a standstill budget, any revenue package will likely be centered around renewing part of the "clean penny."

The story so far

The Legislature is barred by the constitution from raising taxes during even-numbered "regular session" years. But they still have to pass a budget using only the revenue available. The Legislature has now made four separate attempts to craft a 2018-19 budget without new revenues. All four of these versions of the budget made deep cuts to vital programs:

- The version passed by the House Appropriations Committee included full funding for TOPS scholarships. But it cut more than $680 million in state support for Medicaid. When this funding goes away, so does the federal matching dollars that also supports health care services in Louisiana for a total cut of more than $2.4 billion. This would force teaching hospitals to close and resulted in tens of thousands of people losing Medicaid coverage. The state's chief economist estimated the reduction in Medicaid funding would cost the state 57,000 jobs.
- The version that passed the full House plugged $92 million back into health care programs by taking it from TOPS, which would have been funded at 80 percent of current levels. But it still left deep cuts to public-private partnership hospitals, mental health services, nursing home eligibility and community-based services for people with disabilities. With federal funds included, the health care cuts totaled $1.8 billion.
- The version crafted by the Senate Finance Committee restored virtually all of the cuts to the Louisiana Department of Health. But in doing so they eviscerated virtually every other part of state government through a 24.2 percent cut in state general fund support. This "pretend budget" eliminates the state food stamp program and makes deep cuts to child welfare services, higher education, assistant district attorneys and veterans services. It also makes it likely that many of the 16,000 state inmates who are serving time in local jails will have to be furloughed.
- The full Senate then ratified this budget, making very few changes.

The Senate's "pretend" budget is the version that made it to Gov. John Bel Edwards' desk, where it was vetoed.

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Potential solutions:

Option	Explanation	Annual Revenue
Make part of the "5th penny" permanent	Partial renewal of the 1 percentage-point increase in the state sales tax approved in 2016, without exemptions.	$218 million per .25%
"Clean" the other four pennies	Remove exemptions from permanent 4% state sales tax and charge a 2% sales tax on utility bills for manufacturers and a 4% tax for other businesses.	$115 million. If all "business inputs" were taxed at 2%, it would raise only $70 million.
Ending the "double deduction"	Louisiana is one of only five states that allows taxpayers to deduct their prior year's state income-tax payments on their tax returns.	$79 million
Credit for taxes paid to other states	A 2015 law, which expires June 30, limits the amount of a tax credit people can claim for income taxes paid to another state. The law restricts the credit to states that provide a similar credit for people who pay tax in Louisiana.	$34 million
Corporate deductions	A 2015 law limits certain deductions that corporations can take to reduce their taxable income in Louisiana. The law expires June 30.	$16.5 million
BP settlement	Louisiana will receive $53.3 million per year from BP for 15 years starting in FY19 for economic damages resulting from the 2011 Deepwater Horizon spill. The money currently goes to three state trust funds.	$53.3 million

While the revenue options listed above are considered the most likely to gain the votes necessary to pass the House and Senate, there are other ways to help solve the fiscal cliff:

- "Shrinking" the brackets for personal income taxes to the way they were from 2003 to 2009, and limiting the itemized deductions that people can claim on their state returns: $543 million.
- Reducing the annual cap on film tax credits, from $180 million to $135 million: $45 million.

Unfortunately, any revenue package that relies mostly on sales taxes will hit low-income households the hardest, which is why the Legislature should couple any sales-tax measure with an increase in Louisiana's Earned Income Tax Credit.

-Jan Moller