

MISSISSIPPI STATE BUDGET BASICS IN 2011

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Thousands of jobs in local education have been lost as a result of the fiscal crisis facing state and local government in Mississippi. The squeeze on the state budget, unfortunately, is expected to continue for a while. This article provides an overview of the state budget and cites sources where further information can be found that would be useful in examining both the expenditure and revenue sides of the state budget.

Table 1 shows the fall in **state expenditures** by category in FY2009 for the total budget, general and special funds combined. Public education funding was reduced 1.9% in FY2009, higher education 4.0%, and local assistance 12.4%. Funding reductions were also suffered by hospitals, agriculture/commerce/economic develop-

ment and public works. Part of the funding loss, for example, in economic development, was due to a fall in federal funds after Katrina disaster assistance ended.

Still, because of the recession, the level of state spending in FY2010 was even lower than in FY2009. At the same time, **financial demands** on the state continue to rise: debt service, Medicaid, and state employee retirement benefits are among the obligations that have been increasing. (Medicaid rolls are rising as more people qualify for the program; the state provides the funds required to draw down the federal match, which currently is more than four federal dollars for every state dollar.) To meet rising obligations in some areas, cuts must be made in others.

Table 1. STATE GOVERNMENTAL EXPENDITURES, COMBINED GENERAL AND SPECIAL FUNDS
Fiscal Year 2009

	Millions of Current \$	Percent of Total	% Change FY2008-FY2009
Public Education	\$3,063.5	19%	-1.9%
Higher Education	\$955.3	6%	-4.0%
Health and Social Welfare	\$5,697.1	35%	16.3%
Hospitals/Hospital Schools	\$585.2	4%	-5.0%
Corrections and Justice	\$461.7	3%	0.3%
Agric/Commerce/EconDev ¹	\$975.8	6%	-12.4%
Local Assistance	\$914.5	6%	-12.4%
Public Works	\$1,330.7	8%	-6.5%
Other	\$2,227.5	14%	6.9%
Total Expenditures ²	\$16,211.0	100%	2.9%

¹There was a large increase in federal funds in this category post-Katrina, and the 12.4% drop-off shown here is due to reduction in federal funds.

²Sum may not total 100% due to rounding errors.

SOURCE: Mississippi Center for Policy Research and Planning. *Mississippi Fiscal Summary*, January 2010 at www.mississippi.edu/urc.

Table 2. REVENUE SOURCES, MISSISSIPPI STATE BUDGET FY2009

	<u>2009</u>	<u>Percent of Total</u>
Taxes		
Sales and use ¹	\$3,008,042	20%
Gasoline and other motor fuel	\$412,206	3%
Individual Income	\$1,441,141	10%
Corporate income and franchise	\$420,482	3%
Insurance	\$187,050	1%
Gaming	\$172,429	1%
Other	\$288,635	2%
Licenses, permits, charges for services	\$878,717	6%
Federal government	\$7,402,207	50%
Other	\$634,840	4%
Total Revenues	<u>\$14,845,749</u>	<u>100%</u>

Note: Modified Accrual Basis of Accounting (Expressed in Thousands)

¹General and special funds.

SOURCE: Mississippi Department of Finance and Administration. *Comprehensive Annual Fiscal Reports 2010* at www.dfa.state.ms.us.

Stimulus funding under the American Recovery and Reinvestment Act (ARRA) has provided Mississippi (state and local government) with \$2.7 billion for specified programs; as of November 2010, Mississippi reported that it has received \$1.2 billion of these funds.¹ But the stimulus funds supporting the state budget end in 2012, and this is a major reason why Mississippi's proposed FY2012 General Fund budget is little changed from that of FY2011.

The story will not end in FY2012. A **severe budget squeeze** is expected to continue into FY2013 and, even after that, Mississippi will suffer a declining fiscal position, in line with predictions made by the Government Accountability Office (GAO) and other experts for most state budgets. The GAO (2010) sees health-related costs as the primary driver of the predicted recurrent shortfalls. (See the June 2010 issue of the *Review* for an overview of the complexities involved in controlling health care costs.)

Performance-Based Budgeting

Balancing the state budget, then, will be an on-going challenge facing the state. As a result, the renewed interest in performance-based budgeting is of particular importance. Performance reviews enable the streamlining of programs, elimination of waste and duplication, and a more careful targeting of budget cuts. The use of across-the-board cuts of a given percentage, impacting all categories equally, is inefficient; such cuts can have devastating effects in some areas, while other programs may be well-positioned to weather such cuts. (The June issue of the *Review* (pages 25-27) provides information on several studies addressing the specifics of performance reviews. Appendix B, Tables 10 and 11, at the back of this *Review* provide more details on revenue and expenditure trends in the state since 1999.)

Tax Reform

Of course, tax reform will be on the agenda as well, as another means of

reducing budget shortfalls. Table 2 gives the major sources of funds financing the annual state budget in FY2009. Note that federal funds accounted for 50% of the total. These funds are critical to the state and have been increasing in importance, even after taking into account the temporary spike in federal funds received post-Katrina, FY2006 to FY2008. So, for example, most of the \$5.7 billion spent on health and social welfare in FY2009 was financed by the federal government: about \$2.9 billion in federal funds went to Medicaid; \$750 million to Human and Rehabilitation Services and \$200 million to public and mental health. Not shown is the break-down between special fund and general fund revenues. Suffice it to say that state-source special funds, \$3.1 billion in FY2009, are approaching general fund revenues, \$4.6 billion that year, in value.

As Table 2 shows, the most important generators of tax revenue for the state are the sales and income taxes. Mississippi's 7% general sales tax rate was the second highest in the country, after California; many states allow cities to charge a local sales tax as well, which can bring up the overall tax rate.²

Per capita general sales tax revenues were \$1,080 in 2007, ranking Mississippi 7th highest in the nation. Mississippi also has taxes on beer, wine, tobacco, liquor, motor fuel and use taxes, which are all forms of sales tax. **Per capita revenue from the individual income tax** was \$480 in 2007, ranking Mississippi 41st in the country. Per capita revenue from the state tax on net corporate income was \$126 in 2007, ranking the state 34th in the nation.³

Although Mississippi's general sales tax rate is 7%, there are different rates on such items as manufacturing machinery (1.5%) and contracting sales (3.5%). The *Summary Comparison of State Taxes in Selected Southeastern States* describes the state sales

tax rates and exemptions in detail. The individual income tax is the second largest generator of general fund revenues. There is a 3% tax rate on the first \$5,000 of an individual's taxable income, 4% on the next \$5,000 and 5% on all taxable income over \$10,000. There is a \$6,000 exemption for single individuals, \$12,000 for married couples, and \$1,500 for each dependent. Further description is in the *Summary Comparison*.

The corporate tax is a combination of the income tax and franchise tax paid by corporations. "The corporate income tax is levied at the same rates that apply to the individual income tax. The franchise tax is levied at \$2.50 per \$1,000 capital employed in the state, or the assessed valuation of property in Mississippi, whichever is greater," states the *Mississippi Fiscal Summary 2010*. Many exemptions and incentives are offered to corporations. For example, the **Advantage Job Incentives Program** typically provides the firm with a rebate of a certain percentage of state personal income taxes withheld – the percentage may be as high as 90% or as low as 70%, depending on the average wage paid.⁴

Although it makes sense to start with examining the three major taxes, there are other taxes and **alternative means of revenue-raising** – for example, fees can be increased on government-supported services, such as those of the Department of Environmental Quality or of regulatory agencies; similarly, fees and fines imposed to discourage or penalize certain kinds of behavior can be raised, or introduced; and user fees on such state-owned assets as roads and parks can be increased.

Mississippi state taxes are described in detail and compared to taxes in other states in *A Summary Comparison of State Taxes in Selected Southeastern States*, published by this office and available on-line. *The*

State Tax Base

The state's tax base consists largely of the income generated within the state and wealth held by residents of the state; nonresidents passing through the state do contribute to that base to some extent. The income generated in the state is simply the state's gross domestic product from the income side. The **gross state product** is broken into: wages & salaries, 44%; labor benefits, 11%; gross operating surplus, 38%; and certain taxes on production (not income taxes), 7% (2008 data).⁶ On the other hand, if we look at general fund revenues, the sales tax accounted for 40% of total Tax Commission transfers; the personal income tax, 32%; the corporate income tax, 10%; and the use tax, 4%.

Even though some of the sales tax is paid by businesses, maybe as much as 20% of the total, and some of the personal income tax by small businesses (proprietorships), it remains true that individuals provide considerably more of general fund revenues than do corporations and businesses directly, more than their share in state income. **Detailed information** on who in Mississippi pays how much in federal income taxes is available from the Internal Revenue Service and is provided in the appendix table at the end of this article. Similar information is not available from the Mississippi Department of Revenue.

Wealth (that is, property and other assets) is subject to taxation primarily through local property taxes in Mississippi, although the corporate franchise tax discussed above is also a form of property tax. Property taxes per capita here were \$717 in 2006, which ranked Mississippi 41st in the nation. Franchise and/or estate taxes could augment state revenues, as could taxes on the use or extraction of state resources.

Annual Tax Expenditure Report, also published by this office and also available on-line, gives a comprehensive list of exemptions and tax reductions provided by the state tax code for the different state taxes. More can be found out about the state unemployment insurance tax, which funds the Unemployment Insurance Trust Fund, in the June 2009 issue of this *Review*.⁵

Concluding Remarks

Improvement of the state's fiscal position will require examination of both expenditures and revenue sources. The information above provides an overview of the state budget and gives sources where further information can be found.

Should Mississippians decide that more revenues are needed to finance state programs, the principles of equity, stability

and efficiency can provide useful guidance for their decisions. Discussion of these principles and of tax alternatives is provided in “The State Budget: The Road Ahead” (December 2008 issue of this *Review*). In general, states can find stable, equitable revenue sources when they levy taxes in line with their distributions of income and wealth.

The more information taxpayers and officials have on individual government programs – their costs and achievements – and on actual and potential individual revenue sources – their costs to individuals and businesses and their impacts on efficiency and competitiveness – the better the decisions that can be made and so the better the functioning of the state government will be.

Notes

1. See www.recovery.gov and www.stimulus.ms.gov. Under the American Recovery and Reinvestment Act, Mississippi’s state and local governments will receive over \$2.7 billion. In addition, tax relief will likely total more than a billion dollars – substantially more if Mississippians take advantage of tax credits for green energy, college and other new tax breaks. And government agencies and private firms will have access to billions set aside for grants to encourage investment in broadband, smart electricity grids, Superfund clean-ups, health information systems, renewable energy, greener transportation, and more. Federal agencies, such as the Department of Homeland Security, the Department of Defense and the Army Corps of Engineers, are also receiving funds for projects in the state. See p. 17 of the June 2009 *Review* for more detailed information.

In 2009, Mississippi was awarded \$479 million for fiscal stabilization under the American Recovery and Reinvestment Act (ARRA) stimulus plan (this has largely been spent) and \$779 million for Medicaid funding in FY2010 and FY2011. An additional \$127 million, provided in 2011 for Medicaid, will be used by the state in FY2012, according to an August 31, 2010 press release from the Governor’s office.

Data from the official U.S. government website tracking stimulus spending provides the following breakdown of funds coming to Mississippi. Some of

the grants awarded have undoubtedly been included as part of the funding of some state agencies in the FY2011 state budget, even though the funds have not yet been received and/or there is some lag in reporting.

Mississippi	Contracts	\$577,669,119
	Grants	\$2,128,085,384
	Loans	\$35,075,557
	Total	\$2,740,830,060

2. State Tax Administrators.

3. Morgan and Morgan (2009).

4. To lure the Toyota plant, for example, the state offered \$326 million in incentives with local government chipping in another \$30 million. Most of the incentives, as detailed in Senate Bill 3215 (2007), will go to infrastructure (\$162 million) and site preparation (\$50 million). Another \$84 million is for job training and an on-site training facility, plus \$30 million to training for suppliers at two community colleges and the University of Mississippi. In addition, Toyota is eligible for income tax exemptions, reduced taxes in other areas, and may receive rebates on payroll taxes, sales and use taxes on equipment used to build vehicles, and contractor taxes on the plant’s construction. These will add millions to the package.

For a complete list of incentives provided to Toyota, see Senate Bill 3215, regular session 2007, at www.ls.state.ms.us. A description of incentive packages is at www.mississippi.org. Under loan programs for business, see especially Mississippi Major Economic Impact Authority. The incentives under the Advantage Job Incentives Program apply if the annual average wage is at least 125% but less than 175% of the lesser of the average county or state wage; then the rebate is 80% of those withheld taxes (but no more than state personal income taxes actually paid by employees).

Several states conduct on-going evaluation of business incentives, and charge a surtax or modify agreements as conditions warrant.

5. The funds from the state Unemployment Insurance (UI) tax go into a trust fund used to finance unemployment benefits and so has not been a part of the discussion about balancing the state

budget. Any increase in unemployment benefits would be funded through changes in this tax. The average UI payroll tax rate in Mississippi is about 1.84% and it is levied on the first \$7,000 of pay only; it amounts to about \$129 per worker per year ($\$129 = .0184 \times \$7,000$). The rate varies between firms and also from year to year as a result: it is somewhat higher for firms that have more frequent layoffs. The maximum rate is 5.4% and the statutory minimum is 0.7%, according to 2009 data.

The tax base of \$7,000 was set in 1983, when the tax rate ranged from 3.1% to 4.0%. If the tax base were adjusted for the inflation that has occurred since 1983, the base would be \$15,267. (Prices of consumer goods and services more than doubled between 1983 and 2010, based on the consumer price index.)

6. Data on operating surplus of the government sector versus private industry was not readily available for 2008. However, in 2006, of the 35% going to GOS, the percentage to private industry was 33% and to government 2%. The gross operating surplus includes pre-tax profits, capital consumption (depreciation), net interest payments and some taxes (but not on income), and does not include the cost of inputs used in production. (The use tax, paid largely by businesses, accounted for 5% of GF transfers in FY2006 and 4% pre-Katrina.) Businesses deduct their costs of production in calculating their net incomes, while individuals are allowed some deductions and an exemption of \$6,000 (for single filers) or \$12,000 (married couples) in determining taxable income.

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Appendix Table. **FEDERAL INDIVIDUAL INCOME TAX DATA FOR MISSISSIPPI 2008**

	All Returns	<u>Percentage of Total By Size of Adjusted Gross Income</u>				
		Under \$50,000	\$50,000- \$74,999	\$75,000 - \$99,999	\$100,000 - \$199,999	\$200,000 or more
Number of Returns	1,254,942	74.4%	11.5%	6.4%	6.1%	1.5%
Adjusted Gross Income (millions)	\$52,322	32.8%	16.9%	13.3%	19.0%	18.0%
Taxable Income ¹ (millions)	\$32,722	21.0%	17.1%	14.8%	22.7%	24.4%
Income Tax (millions)	\$5,250	12.2%	12.9%	12.1%	24.1%	38.7%
		<u>Effective Tax Rate</u>				
Tax/Taxable Income	16.0%	9.3%	12.1%	13.1%	17.1%	25.4%

¹Taxable income equals adjusted gross income minus deductions but before tax credits.
SOURCE: Internal Revenue Service, *Statistics of Income, 2010*.