Fiscal and Economic Analysis of HB 1

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This report presents URC's fiscal and economic analysis of HB 1, the "Build Up Mississippi Act," as passed by the Mississippi state legislature and signed into law by Governor Tate Reeves on March 27, 2025. URC used the Tax-PI software, a dynamic fiscal and economic impact model produced by Regional Economic Models, Inc., to conduct this analysis. Importantly, this report makes no recommendations in support of or in opposition to HB 1; rather, the goal of this report is to provide information on the expected fiscal and economic impacts of the bill following its enactment.

Specifications of HB 1

HB 1 primarily consists of the following provisions:[1]

- Reduces the 4.0% individual income tax rate [as of tax year 2026] annually beginning with the 2027 tax year. The rate falls to 3.75% in the 2027 tax year, to 3.5% in tax year 2028, to 3.25% in tax year 2029, and then to 3.0% beginning with the 2030 tax year.
- Beginning in tax year 2031, if general fund revenue exceeds appropriations for the following fiscal year by 0.85% but less than 1.0% of the value of 1 percentage point of individual income tax revenue, reduces the individual income tax rate by 0.2%; if general fund revenue exceeds appropriations for the following fiscal year by at least 1.0% but less than 1.15% of the value of 1 percentage point of individual income tax revenue, reduces the individual income tax rate by 0.25%; if general fund revenue exceeds appropriations for the following fiscal year by at least 1.15% of the value of 1 percentage point of individual income tax revenue, reduces the individual income tax rate by 0.3%.
- Reduces the 7.0% sales tax rate on grocery items (non-prepared foods) to 5.0% as of July 1, 2025.
- Increases the current diversion of 18.5% of sales tax revenue collected on grocery items (at the current 7.0% rate) to municipalities to 25.9% effective September 15, 2025.
- Increases the current state excise tax on gasoline of 18 cents per gallon to 21 cents per gallon effective July 1, 2025; to 24 cents per gallon effective July 1, 2026; and to 27 cents per gallon effective July 1, 2027. Effective July 1, 2029, HB 1 also adjusts the excise tax on gasoline for inflation according to the National Highway Construction Cost Index (NHCCI) produced by the U.S. Federal Highway Administration. This adjustment is limited to 1 cent per gallon per year and takes effect every other year. Transfers 74% of the additional revenue generated from the increase in the excise tax to the Mississippi Department of Transportation, 23.25% to the Office of State Aid Road Construction, and 2.75% to the Strategic Multi-Modal Investments Fund, the latter of which is created by the bill.

HB 1 does not stipulate a date for full implementation, as this date could vary depending on revenues collected. However, for simplicity our analysis assumes the individual income tax rate will decrease by 0.3% annually beginning in tax year 2031 until tax year 2040, when the rate will equal zero. This year represents the earliest possible date HB 1 could effectively eliminate the individual income tax. Therefore, under our assumptions once fully implemented in 2040, HB 1 effectively eliminates the Mississippi individual income tax, sets the sales tax rate on grocery items at 5.0%, and sets the excise tax on gasoline at 27 cents per gallon, subject to future adjustments for inflation.

[1] HB 1 also makes changes to the Public Employees Retirement System in Mississippi by creating an additional tier for new state employees. However, as this change affects employees who will be hired in the future, it is beyond the scope of our analysis of changes in tax laws and therefore is not incorporated into this report.

Revenue impacts of HB 1

In assessing how HB 1 affects revenues collected by the state, we acknowledge two points at the outset of our analysis. First, HB 1 directly impacts revenues transferred to the general fund through its reduction and ultimate elimination of the individual income tax and the reduction of the sales tax on grocery items to 5.0%. Second, the bill impacts revenues collected by the state *outside* of the general fund through its increase of the excise tax on gasoline to 27 cents per gallon. We discuss this latter change in the context of *total* revenues collected by the state, but this change is not directly incorporated into our analysis of the impact of HB 1 on *general fund* revenues.

Our baseline scenario represents a continuation of current law. In this scenario general fund revenue increases by an average of 3.3% per year from FY2026 through FY2040. This overall growth rate in general fund revenue results from the annual growth rates we assume for major revenue sources, which include: 3.0% per year for sales tax revenue, 3.5% per year for individual income tax revenue, 3.1% per year for corporate income tax revenue, and 3.1% for use tax revenue. These rates that we assume are conservative and in line with historical averages. This scenario assumes that no additional laws that impact general fund revenue sources are enacted before 2040.

Our scenario for HB 1 reflects the *total* changes in general fund revenue each year from the provisions of the bill and captures both the direct and indirect effects of the reductions in taxes as estimated by the Tax-PI model. These values essentially capture the economic effects of changes in tax rates as mentioned above. Because of these effects, the total decreases in general fund revenues each year are less than the direct decreases in general fund revenues that result from changes in taxes. The changes in taxes under HB 1 that directly affect general fund revenue include the decreases in income tax rates and the decrease in the sales tax rate on grocery items.

The total decreases in general fund revenues are less than the decreases in taxes each year as spending by individual taxpayers increases due to the increase in income from the reductions in taxes. The state collects sales and use tax revenue on this additional spending on taxable goods, and these additional sales and use tax revenues partially offset the decrease in revenues from the income tax reductions. In addition, the amount of sales tax revenue transferred to the general fund is reduced each year due to the economic effects of the increases in the excise tax on gasoline. That is, the model captures the decrease in revenue transferred to the general fund from residents who spend less overall because of the effective higher prices caused by the increase in the gasoline tax. These impacts are relatively small. URC estimates in FY2040 the state will collect approximately $3.0 billion less in general fund revenue compared to the current baseline because of the provisions of HB 1. In our analysis the average increase in general fund revenue from FY2026 to FY2040 under HB 1 is 0.6% per year.

In addition to the changes in general fund revenues we estimate, we recognize HB 1 generates additional revenue outside of the general fund. HB 1 enacts a 3 cents-per gallon tax on gasoline in FY2026, FY2027, and FY2028. The bill's authors estimate this tax will generate $212 million annually. If this tax grows at an average annual rate of 3.0%, like sales tax revenue, then by 2040 this tax could generate approximately $310 million per year. This revenue could experience modest additional growth in future years since the increase in the excise tax is adjusted for inflation, as noted in the bullet points above. The bill transfers 74% of this increase in the excise tax to the Mississippi Department of Transportation. Secondly, we acknowledge that as of January 2025, based on the recommendation of the Joint Legislative Budget Committee (JLBC), the state will have approximately $2.5 billion in reserve funds at the end of FY2026[2]. These funds could be used to offset the annual decreases in general fund revenues for several fiscal years following the implementation of HB 1, if legislators chose to do so. However, if these funds are used to offset the annual decreases in general fund revenue, they

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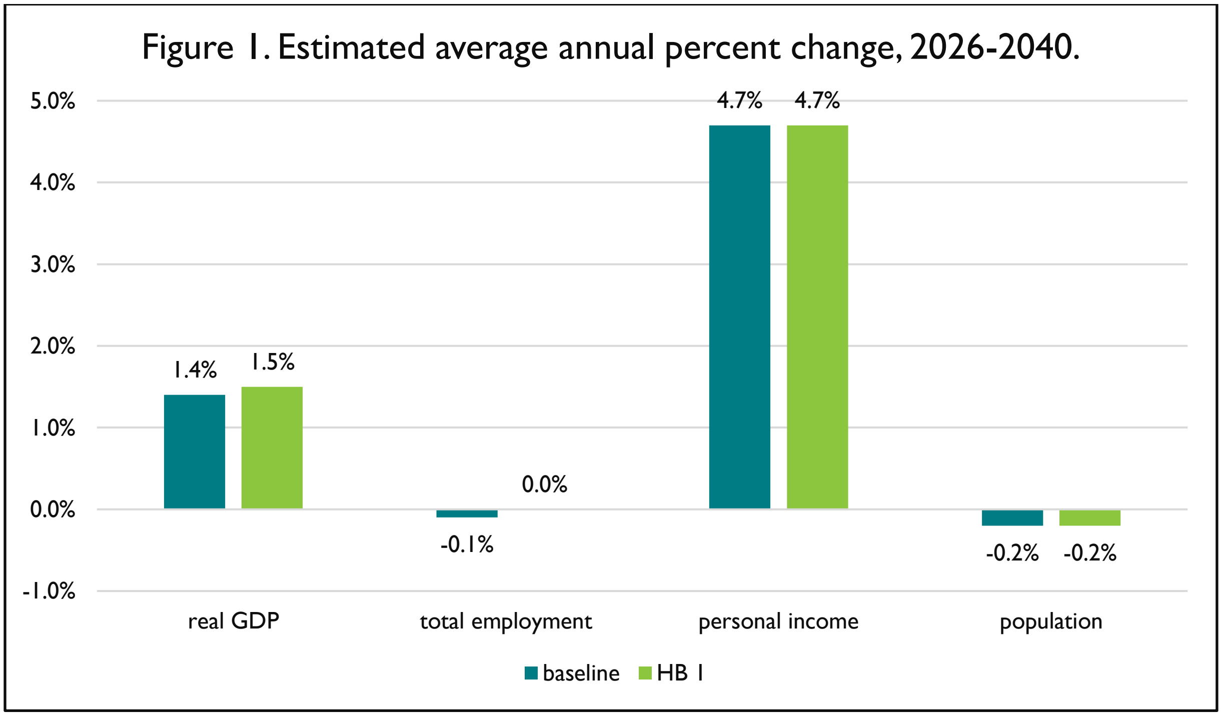
[2] See "FY 2026 Mississippi Legislative Budget Recommendation Report," page 9, available at: https://www.lbo.ms.gov/PublicReports/GetBudgetRequestDetailReport/0?report=Intro&fiscalYear=2026.

will likely be depleted by FY2030. In summary, under HB 1 the reduction and ultimate elimination of the individual income tax and the reduction in the sales tax on groceries results in a decrease in general fund revenue. An increase in gasoline excise taxes generates additional revenues to the state outside of the general fund.

Economic impacts of HB 1

URC estimated impacts to the Mississippi economy from the provisions of HB 1 for calendar years 2026 through 2040. These changes are in addition to or on top of the baseline changes expected each year and reflect the changes that occur solely due to HB 1. The economic variables we estimate using the Tax-PI model include real[3] gross domestic product (GDP), total payroll employment, personal income, and population. Figure 1 below depicts the average annual growth of each of these variables in the baseline scenario and under HB 1.



Source: URC estimates.

In the baseline scenario, real GDP for Mississippi grows by an average of 1.4% per year from 2026 through 2040. Under HB 1, the average growth over this period is 1.5% per year. In 2040, real GDP for Mississippi is 0.3% higher under HB 1 compared to the baseline scenario of the Tax-PI model.

Total payroll employment for Mississippi changes by an average of -0.1% per year from 2026 through 2040 in the baseline scenario. Over this same period under HB 1, the average annual change in total payroll employment for the state is 0.0%. The Tax-PI model projects that in 2040, total payroll employment for Mississippi is 0.3% higher under HB 1 compared to the baseline scenario.

[3] The GDP values are expressed in 2017 dollars, which means they are real values that have been adjusted for inflation using 2017 as a base year.

In the baseline scenario, personal income for Mississippi grows by an average of 4.7% per year from 2026 through 2040. Under HB 1, the average growth over this period is also 4.7% per year. In 2040, personal income for Mississippi is 0.4% higher under HB 1 compared to the baseline scenario of the Tax-PI model.

Finally, the total population of Mississippi changes by an average of -0.2% per year from 2026 through 2040 according to the baseline scenario. The average annual change in the state's population over this same period is also -0.2% under HB 1. However, in 2040 the total population for Mississippi is 0.8% higher under HB 1 compared to the baseline scenario.

As we noted previously, based on the recommendation of the JLBC as of January 2025 the state will have approximately $2.5 billion in reserve funds at the end of FY2026; if legislators chose these funds could be used to offset decreases in general fund revenues in the first few fiscal years following the implementation of HB 1. If the Mississippi legislature chose to use these additional funds to partially offset the decrease in individual income tax revenues that results from implementation of HB 1, then the economic impacts of each variable in Figure 1 would increase by relatively small amounts. The largest increases likely would occur in total payroll employment if more of the decreases in the state's expenditures were offset.

Welfare impacts of HB 1

A complete evaluation of individual welfare impacts is beyond the scope of this analysis; however, we highlight a few aspects of HB 1 regarding tax incidence. First, as other URC publications have noted, despite the move to a single rate as of tax year 2024 the individual income tax in Mississippi remains slightly progressive. The elimination of the 3% and 4% tax brackets means no tax is levied on annual taxable income of $10,000 and below. Furthermore, as of tax year 2024 the personal exemption of $6,000 and the standard deduction for an individual of $2,300 mean an individual pays no income tax on the first $18,300 of taxable income. The gradual elimination of the individual income tax under HB 1 removes this progressivity from the tax code. Second, economists consider sales taxes as well as excise taxes regressive because, by definition, the share of income paid in sales taxes decreases as an individual's income increases. The reduction of the sales tax rate on groceries mitigates some of this regressivity. However, the 9 cent-per gallon increase in the excise tax on gasoline–a tax that is also regressive–increases the regressivity of the individual tax code. Nevertheless, the decrease in the sales tax on grocery items and the increase in the excise tax on gasoline represent relatively small changes. We expect for most individuals in the state the changes in welfare caused by the changes in these two taxes will likely offset one another. We do expect most if not all individuals who file individual income taxes in Mississippi will pay less in total taxes under HB 1. In our judgment, because the current individual income tax in Mississippi is somewhat progressive, its elimination under the bill means the regressivity of the state's individual tax code is likely to increase under HB 1.

Summary of HB 1

In conclusion, URC's analysis of HB 1 finds that, compared to a baseline scenario, general fund revenue on average grows less per fiscal year from FY2026 through FY2040. Under HB 1, general fund revenue grows by an average of 0.6% per fiscal year from FY2026 through FY2040, compared to an average of 3.3% per year in our baseline scenario. The decline in general fund revenue growth results primarily from the reduction and ultimate elimination of the individual income tax, and, to a lesser extent, the reduction in the sales tax on grocery items. Our analysis projects that in FY2040, the final year we evaluate and the earliest date the individual income tax could be eliminated, general fund revenue will be approximately $3.0 billion less under HB 1 compared to the baseline scenario. HB 1 will also generate additional revenues outside of the general fund in the form of additional gasoline taxes that should be accounted for when considering its net impact on revenues collected by the state.

In terms of economic impacts, we find real GDP for the state under HB 1 increases by an average of 1.5% per year from 2026 through 2040, compared to an average of 1.4% per year in the baseline scenario. Real GDP for Mississippi in 2040 is 0.3% larger under HB 1 compared to the baseline scenario. Similarly, total payroll employment on average is unchanged each year from 2026 through 2040 under HB 1, whereas in the baseline scenario payroll employment decreases by an average of -0.1% per year over the same period. Total payroll employment in the state is 0.3% higher in 2040 under HB 1 compared to the baseline scenario. URC finds personal income in the state will increase by an average of 4.7% per year from 2026 through 2040 under HB 1, the same rate as in the baseline scenario. In 2040, personal income in Mississippi is 0.4% higher under HB 1 compared to the baseline forecast. Finally, our analysis finds the population of Mississippi decreases by an average of -0.2% per year from 2026 through 2040 under HB 1, the same as in the baseline scenario. Nevertheless, the state's population in 2040 is 0.8% higher under HB 1 than in the baseline scenario.