**TASK FORCE ON STRUCTURAL CHANGES IN BUDGET AND TAX POLICY**
**SUMMARY OF RECOMMENDATIONS**

The Task Force on Structural Changes in Budget and Tax Policy started with the premise that a tax structure should generate sufficient revenues to fund legitimate and necessary government expenses and, in doing so, should be fair, simple, competitive with other states, and stable over the short and long term. These qualities are best achieved with taxes that are broad-based with low rates and that do not play favorites for or against a particular constituency; however, the Task Force viewed economic competitiveness and comparisons to other states as fundamentally relevant factors in its decision making, while attempting to assure that compliance with a new structure would be easy and clear. The Task Force also believes that exceptions should be minimal and for clearly established good reasons that serve our state's needs.

The Task Force acknowledges that much of what the state spends each year is constitutionally and statutorily obligated before the Legislature begins the budget debate and is primarily required to meet fundamental state obligations. The Legislature is limited in its ability to alter the spending obligations and there are few clearly identifiable areas that can easily be eliminated to materially reduce overall state spending. Additionally, a substantial portion of the state budget is derived from federal matching funds that cannot be utilized for anything other than the designated purpose. However, there are areas that should be addressed to provide for better budgeting practices and to prevent overspending, which would mitigate the potential for mid-year deficits, allow for better long-term planning and potentially free up revenues to address long-standing accumulated state obligations.

The Task Force offers the following recommendations that should be considered as a package. Although the changes will require separate pieces of legislation, they should be considered in their entirety as a whole and not individually in isolation, because of their interactions with one another in establishing a balanced and fair tax system. With that in mind, the Task Force - after more than six months of information gathering and deliberations - makes the following recommendations:

**BUDGET AND SPENDING RECOMMENDATIONS**:

1. Avoid budgeting practices that allow for spending beyond available recurring revenues.

2. Implement and adhere to improved revenue forecasting, particularly with regard to the MFP, Medicaid and TOPS, that more closely predicts actual utilization. The state should consider establishing a formal multi-year spending forecast for such things as Medicaid, the MFP, TOPS and Corrections.

3. Continue the ongoing review of state contracts to identify opportunities for consolidation, renegotiation or elimination.

4. Examine individual constitutional dedications to determine if they remain a state policy priority.

5. Conduct a holistic review of state trust funds for possible revision, elimination or merger of funds.

6. Continue to implement fiscal structures that will help protect the state budget from swings in volatile state revenue streams, such as mineral revenues and corporate taxes.

7. Implement staggered sunsets on all statutory dedications to see if they can be adjusted, eliminated or combined with others.

8. Continue payments to state pension systems on the initial Unfunded Accrued Liability under the current timeline to avoid increasing debt, while looking for ways to accelerate payments toward an earlier debt retirement.

9. Examine expected rates of return on pension investments to make proper adjustments to ensure that the retirement systems are not creating another new and costly unfunded accrued liability in the future.

10. Continue review of various tax credits, rebates, deductions, and exemptions to state taxes to determine whether they can be eliminated, curtailed or more closely regulated.

**SALES TAX RECOMMENDATIONS:**

1. The Task Force recommends expanding the sales tax base and reducing the sales tax rate from its current 5 percent to no more than 4 percent. To do so, the Task Force recommends: (1) retaining, with a few modifications, the expanded state sales tax base adopted in Act 26 of the first special session of 2016 and amended by Act 12 in the second special session, which would continue the tax on such things as custom software, business utilities, and storm shutter devices; and (2) making certain services, such as those taxed in Texas, and digital transactions subject to sales tax. Some of the taxable services include cable and satellite television, repairs to nonresidential, commercial property, web hosting and security services.

2. The Task Force recommends that the state should take meaningful steps to establish a more uniform sales tax base by bringing exemptions and exclusions in line on both the state and local levels.

3. The Task Force recommends that the state and local governments work to create a uniform system of tax administration, collection and audit that respects and protects local revenue streams from any overlap with state revenues.

4. The Task Force recommends allowing local governments the ability to increase their sales tax rates without a vote of the state Legislature, but still requiring a vote of the people in the area being taxed. Sales tax and property tax reform are essential if local governments are to have the tax capacity to independently provide their own funding.

5. In order to provide greater clarity and ease of compliance, the Task Force recommends a recodification of sales tax law.

**INCOME TAX RECOMMENDATIONS:**

1. The task force recommends eliminating the state deduction for federal income taxes paid, accompanied by appropriate state income tax rate reductions. This change would decouple Louisiana's income tax base from federal tax changes. It also recommends limiting the excess itemized deduction for personal income to 50 percent. These two deductions account for a reduction of $1.225 billion in income tax collections in Louisiana at the current rate structure. These exemptions provide a much larger tax break to higher income groups, both absolutely and proportionally. If the excess itemized deduction were limited to 50 percent, mortgage interest and charitable giving would still be deductible.

2. The Task Force recommends two options for changes to the individual income tax law under either a constitutional amendment option or a statutory option. A constitutional option allows Louisiana to expand the income tax base, narrow the brackets, and lower all rates by 25 percent. A statutory option only allows base expansion and narrowing of the brackets.

- Under the constitutional option, the Task Force recommends allowing voters to approve the elimination of the federal income tax deduction that decouples the Louisiana tax base from federal tax changes. This option would include scaling back excess itemized deductions to 50 percent. A new three-bracket structure would be used and rates of taxation lowered – 1.5% on the first $25,000 ($12,500 single), 3% on $25,000 through $50,000 ($12,500 through $25,000 single) and 4.5% above $50,000 (above $25,000 single). Not only would rates be lowered by 25 percent, but they would apply more fairly and evenly to all taxpayers because of the proposed elimination of many deductions and exemptions.

- Under the statutory option, the excess itemized deduction would be fully eliminated. This would be coupled with the elimination of other deductions and exemptions proposed by the Task Force. The statutory option would use the new compressed three-bracket structure, but tax rates would remain at the current 2%, 4% and 6% levels.

3. The Task Force recommends the elimination of many income tax exemptions and credits and the imposition of a moratorium on any new tax credits or exemptions applied to the individual income tax. The Task Force recommends keeping (1) the standard and

dependent deductions, (2) the exclusion for military pay for active duty personnel, (3) the credit for taxes paid to another state, (4) the earned income tax credit (because it allows the state to enhance the progressivity of its income tax and reduce the regressive nature of the overall state tax structure), (5) the exclusions for social security and retirement income for public employees, and (6) credits related to child care and early childhood education, in part because these programs help all families and improve educational outcomes, and in part because they leverage federal money.

**CORPORATE TAX RECOMMENDATIONS:**

1. The Task Force supports the proposed constitutional amendment on the November ballot (Amendment No. 3) that would eliminate the corporate income tax deduction for federal taxes paid. The proposed amendment decouples the Louisiana tax base from federal tax changes and provides the opportunity to lower the corporate tax rate. Louisiana's top rate of 8 percent for corporate income taxes is among the highest in the southern and central regions of the country. This change would improve the perception of the state's business climate while also simplifying the tax and broadening the base. If the amendment passes, the corporate tax rate would become a flat 6.5 percent.

2. The Task Force recommends directing the Department of Revenue, with the Louisiana Tax Institute, to study moving from single-entity taxation on the corporate level to a system of combined reporting with findings due by January 2019. Under combined reporting, corporations are taxed based on their apportioned share of income of their "unitary group" which includes a variety of criteria, including common ownership, common management and common lines of business. Combined reporting solves the profit-shifting incentive because related companies are part of a unitary group in which intercompany transactions are eliminated. Instead a state will apportion the entire unitary group using a combined return to determine its share of its tax base.

3. The Task Force recommends restructuring, phasing out or eliminating the corporate franchise tax, provided the state identifies replacement revenue that coincides with the restructuring, phasing out or elimination of the tax. The analysis of whether the restructuring, elimination, or phase out is appropriate, along with the identification of the replacement revenue source, is to be conducted by the Department of Revenue, with the Louisiana Tax Institute. The findings are to be presented to the Legislature by January 2019.

**AD VALOREM TAX RECOMMENDATIONS:**

1. The Task Force recommends amending the Louisiana Constitution to provide local governmental authorities with a role in granting industrial tax exemptions and the creation of a statutory framework to establish the extent of this role for local involvement, as well as

defined policies for use of the exemption as an economic development tool that favors job growth.

2. The Task Force recommends the expanded use of payment in lieu of tax arrangements for local governments considering property tax exemptions to attract economic development. Such arrangements should require the coordinated approval of the elected officials in the impacted taxing jurisdiction.

3. The Task Force recommends the amendment of the Louisiana Constitution to allow for a gradual elimination of locally-imposed inventory taxes over a 10-year period accompanied by the elimination over a five-year period of the state income and franchise tax credit paid on inventory. To offset local governments' reduction in revenues, the Task Force suggests several options, including a constitutional change to allow a roll-up in existing property tax millages, enhanced local revenues resulting from expansion of the sales tax base and changes to the industrial tax exemption, and creation of a temporary revenue sharing fund to bridge the gap as the inventory tax goes away.

4. The Task Force recommends the amendment of the Louisiana Constitution to limit the property tax exemption on property owned by non-profits to that used exclusively for the tax-exempt purposes of the non-profit.

**ECONOMIC DEVELOPMENT INCENTIVE RECOMMENDATIONS:**

1. The Task Force recommends the Louisiana Department of Economic Development (LED) and the Legislature establish sunset review periods for all incentive programs and the elimination of underutilized or inactive programs.

2. The Task Force recommends that LED continue to monitor and regularly report on the performance of all its incentive programs. The reporting must include information on the return on investment for each program and be conducted by independent third parties in accordance with the legislatively established objectives for these programs.

3. The Task Force recommends the retention of the Motion Picture Investor Tax Credit as a non-appropriated, non-refundable tax credit incentive with both discounted redemption and transferability as alternative options for use. The Legislature should implement a modified front-end cap to control the number of credits issued from inception and implement other mechanisms to encourage reasonably timely use to avoid the creation of another backlog of credits that would put a drain on the state budget. The implementation of the front-end cap should coincide with the elimination of the back-end cap.