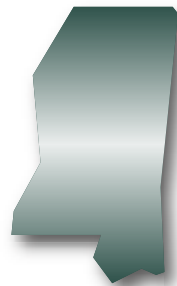




Putting the Pieces Together:
A Taxpayer's Guide
to the Mississippi Budget



Mississippi
Economic Policy
Center

EMBARGO
Until 10:00 A.M.
September 12, 2007

About the Mississippi Economic Policy Center

The Mississippi Economic Policy Center (MEPC) engages in rigorous, accessible and timely analysis to inform the policy debate on issues that affect the economic and social well-being of working families and low-wealth Mississippians. An independent, nonpartisan initiative, MEPC is managed by the Enterprise Corporation of the Delta (ECD), a regional financial institution and community development intermediary dedicated to strengthening communities, building assets and improving lives in economically distressed areas in the Mid South. Key MEPC partners include the Mississippi Center for Justice and other organizations that contribute expertise and otherwise provide important guidance and support.

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To download a copy of *Putting the Pieces Together*, go to www.mepconline.org. To acquire a hard copy of the report, or for other information, contact:

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The MEPC would also like to thank the Legislative Budget Office, the Mississippi State Tax Commission and the Library Commission for their data, guidance and assistance.

Executive Summary

Budget decisions directly influence the quality of education that our children receive, the condition of the roads that we travel, the safety of our communities and the level of trust we can place in professionals such as doctors, dentists, pharmacists and nurses. Of course, each of these services – education, road maintenance and public safety – has a price tag and must be paid for through taxes, fees or borrowed funds. Strong fiscal systems are needed to ensure that the funds are available – in a good economy and in a slow economy – to cover the costs of the services that Mississippi residents depend on everyday.

For Fiscal Year 2008, Mississippi appropriated \$17.4 billion. Nearly half of the appropriated funds came from federal sources (48%) and half from revenue generated from state taxes and fees (52%). To arrive at the funding decisions, important decisions were made to determine how the funds would be spent – and how the funds would be raised to pay for state services. “Putting the Pieces Together” serves as a guide to Mississippi’s budget and tax systems. Divided into five chapters, the guide provides information on:

- The budget process;
- State spending decisions made during the 2007 legislative session;
- How the state generates revenue through taxes, fees and the federal government;
- How to evaluate Mississippi’s tax system; and
- How to get involved in the budget and tax process.

The goals of the report are to increase understanding of the state budget process and to encourage participation in the process for years to come.

Chapter 1: Introduction

Chapter 1 raises the question – why is the state budget important? The budget is important because millions of Mississippians rely on state funded services everyday.

Through state government:

- Over 10,000 miles of roads and bridges are maintained;
- More than 700,000 children are immunized;
- More than 8,000 physicians and 47,000 nurses are licensed by state boards;
- Over 300,000 students are educated by the State Board for Community and Junior Colleges; and
- Nearly 500,000 students are educated through the state’s network of public schools.

Chapter 2: The Budget Process

Chapter 2 provides an overview of the Budget Appropriations Process, through which the state legislature and executive branch work to identify the state’s needs and designate money to fund state services in the next fiscal year. Some key points about the budget process include:

- State services are funded through three primary sources:
 - General Fund dollars raised largely through state income and sales taxes;
 - State source Special Funds raised through fees and special taxes; and
 - Federal source Special Funds sent to the state and earmarked to fund specific programs.
- Leading up to the legislative session, the following entities inform the budget making process:
 - Joint Legislative Budget Committee – hears agency requests in September and submits a budget recommendation to the legislature in December;

- Revenue Estimating Committee – examines economic trends and estimates the amount of revenue that the state will collect in the next fiscal year; and
 - Office of the Governor – submits a budget recommendation to the legislature by November 15.
- All budget recommendations and the final enacted budget must be balanced, and expenditures cannot exceed 98% of the state’s projected revenue without further legislative action.

Chapter 3: A Detailed Look at State Spending

The third chapter highlights the budget decisions made for FY 2008 and examines some trends in state spending. Some of the highlights include:

- The Mississippi Legislature appropriated \$17.4 billion for FY 2008;
- Federal funds accounted for 48% of all the appropriations;
- Most of the appropriations (75%) were for agriculture and economic development, colleges and universities, highways, K-12 education and Medicaid;
- Different state services are funded through different sources. For example:
 - The majority of services funded through Medicaid are funded with federal dollars;
 - Higher and K-12 education are primarily funded through Mississippi tax revenues; and
- Over the last 10 years, state spending has remained stable – increases or decreases in spending have been in line with the state’s economy.

Chapter 4: A Detailed Look at State Revenue

In order to make government work, the state collects revenue from residents and businesses in the form of taxes, fees and funds received from the federal government. Chapter 4 shows how the state generates its revenue. Some key points about state revenue include:

- In FY 2006, Mississippi collected \$13.8 billion in revenue generated mostly through state taxes and federal funds;
- In FY 2006, most (54%) of Mississippi's state tax revenue came from sales and use tax collections – an amount of \$3,074,831,000;
 - Mississippi ranked 7th in the country in the amount of sales taxes paid per resident (\$1,047) in FY 2006;
- Mississippi collected \$1,213,733,000 in personal income taxes – about 21% of its state tax revenues in FY 2006;
 - Mississippi ranked 41st out of 43 states in the amount of income taxes paid per person;
- Mississippi receives a large share of its annual revenue from federal funds – about 50% in FY 2006; and
 - Over the last ten years, the share of federal revenues as a percent of all Mississippi revenues has risen from 38.6% in 1996 to 49.9% in 2006.

Chapter 5: Evaluating Mississippi's Tax System

Chapter 5 introduces some key concepts to be used when evaluating a state tax system and examines the key characteristics of Mississippi's set of taxes. Specifically:

- Healthy tax systems generate enough revenue to pay for services, provide for a fair way of collecting taxes based on one's ability to pay and exhibit a high degree of transparency;
- Mississippi's tax system is regressive –
 - The top 20% of income earners (who earn an average of \$103,400) pay the lowest percentage of their income towards state and local taxes, paying an estimated 7% of their income. The bottom 40% of earners pay the highest percentage of their income towards state and local taxes. The bottom 20% of earners (who earn an average of \$7,000) pay 10% of their income in state and local taxes, and the next 20% of earners (with average earnings of \$15,100) pay 11.5% of their income.
 - Sales taxes are regressive because low-income working families pay a higher proportion of their income on taxes than people with higher incomes; Mississippi relies heavily on the sales tax to generate revenue;
 - Mississippi's sales tax is more regressive than in other states because it taxes groceries – an item that low-income working families cannot avoid purchasing;
 - While mildly progressive, Mississippi's personal income tax functions more like a flat tax – people earning \$30,000 a year are in the same tax bracket as people earning \$250,000 a year; and
 - Working families with wages below the federal poverty line are subject to the state income tax.

Chapter 6: Putting the Pieces Together: How Mississippians Can Get Involved

While the Legislature and the Governor make and approve spending decisions, residents can play an important role in the processes for developing the budget and informing Mississippi's set of taxes. Some ways to get involved include:

- Keep Current – Reading the newspaper and watching the news with an eye towards stories and editorials on state spending and taxes is a good first step;
- Enhance Your Knowledge – If a news story catches one's interest, there are several places to gather additional information on budget and tax topics, including publications released by the Center for Policy Research and Planning at the Institutions for Higher Learning and the Mississippi Economic Policy Center; and
- Engage Others – Connect with other people and organizations engaged in budget and tax work. There are multiple nonprofit organizations in Jackson and around the state that can provide updates on key people, events and votes. The nonprofits can also provide avenues to participate in the process.

This guide provides an overview of Mississippi's budget and tax systems. Given the importance of strong fiscal systems and the funding of vital state services, it is important to understand how the system functions and to ensure that it is efficient and effective.

CHAPTER 1 – Introduction



Why is the State Budget Important?

Every family has a budget. Each month a family brings in a certain amount of income, and each month a family must decide how to spend the money. Some expenses are absolutely necessary — like food, shelter and utilities. Other expenses are much more flexible — like entertainment. During tight months, families face tough decisions about whether cuts in “flexible” expenses must be made. Regardless of whether or not a family uses a formal budget document, each family must plan and account for its needs, often with an income that can’t pay for everything.

The state of Mississippi is no different. It brings money into the state bank account (the Treasury), and the Legislature and the Governor decide how the money will be spent. Just as families must make difficult spending decisions, lawmakers face the same challenge. How does the state fund all the needs and wants of Mississippi residents with limited resources?

While the concept of the Mississippi budget is theoretically similar to that of a family budget, in practice the Mississippi budget can be more puzzling. There are many stages in the state budgeting process, many players that affect the outcome of budget debates, and many sources of revenue — to name just a few complexities. At the end of the day, however, the Mississippi budget provides a blueprint for how the

state government funds services for millions of residents.

Since the state gets its money from the people and is responsible for providing services with that money, the state should be accountable to the people. The state’s budget should reflect their priorities, wishes, and needs.

Budget decisions directly influence the quality of education that our children receive, the condition of the roads that we travel, the safety of our communities and the level of trust we can place in professionals such as doctors, dentists, pharmacists and nurses.

Importance of the State Budget

- Nearly 500,000 students are educated through the state’s network of public schools¹
- More than 300,000 students are educated through the state’s community college system²
- Over 10,000 miles of roads and bridges in all 82 counties are maintained (more miles of road than the distance from Jackson, MS to Melbourne, Australia)³
- Nearly 700,000 individuals receive health insurance coverage⁴
- More than 700,000 infants, children and adults are immunized⁵
- More than 7,000 law enforcement officers are supported in local communities⁶
- More than 24,000 inmates are housed in the state’s correctional system⁷
- More than 8,000 physicians, 3,000 pharmacists, 1,400 dentists, and 47,000 nurses are licensed by state boards⁸

Of course, each of these services — education, road maintenance and public health and safety — has a price tag and must be paid for through taxes, fees or borrowed funds. Strong fiscal systems are needed to ensure that the funds are available — in a good economy or in a slow economy — to cover the costs of the services that Mississippi residents depend on every day.

This report provides a simple overview of how the Mississippi budget is created, how the state spends its money, how it generates revenue, and ways you can get involved in the budget process. Chapters 2 and 3 focus on how the state spends or appropriates its funds. Chapter 4 provides an overview of how the state raises revenue to pay for state services funded by appropriations. In providing a simple overview, the goals of the report are to raise understanding of the state budget process and, we hope, to encourage participation in the budget process in the years to come.

¹ Mississippi Department of Education *2005-2006 Enrollment and Average Daily Attendance Public Schools Report*

² State Board for Community and Junior Colleges *Mississippi Public Community and Junior Colleges Statistical Data 2004-2005*

³ Joint Legislative Budget Committee *State of Mississippi FY 2007 Joint Legislative Budget Report*, Department of Transportation’s agency description

⁴ Office of the Governor Division of Medicaid *FY 2006 Annual Report Summary*, Children’s Health Insurance Program beneficiaries and Medicaid beneficiaries

⁵ Mississippi Department of Health Information Desk webpage http://www.msdh.state.ms.us/msdhsite/_static/4,0,204.html

⁶ United States Department of Justice *DEA Briefs and Background State Fact Sheets, Mississippi 2005*

⁷ Mississippi Department of Corrections *2006 Annual Report*

⁸ Mississippi Board of Nursing *2006 Annual Report*; Mississippi State Board of Medical Licensure website *Table 1: Physicians Licensed*;

Mississippi Board of Pharmacy website *Board Statistics*; Mississippi State Board of Dental Examiners *The Dental Digest* June 2005

The Budget Process



What is the State Budget?

The state budget is the collection of laws, passed each year, that determine how the state collects and spends resources. It includes spending decisions for every service the state provides, and revenue decisions affecting every state resident.

A law allowing the state to spend money is called an appropriation. State appropriations pay for state services like education, criminal justice, and public health. Appropriations are distributed among state agencies with responsibilities for various services. For example, appropriations for education are allocated to the Department of Education, and appropriations for highway construction are allocated to the Department of Transportation.

For Fiscal Year 2008, the Legislature appropriated \$17.4 billion.⁹ This money comprises three kinds of funds:

- **General Funds**
- **Special Funds**
- **Federal Funds**



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General Funds

General funds come from general state tax collections and pay for many key services provided by the state, including K-12 education, colleges and universities, and corrections. The Legislature has significant discretion about how these funds are spent. During strong economic times, the Legislature may use general funds to cover costs associated with new or expanded programs. During weak economic times, general fund appropriations could be cut or held steady to achieve a balanced budget. When the Legislature meets in January, the budget debates that appear in the news mostly revolve around these appropriations.

Special Funds

Special funds are established through state statute or constitutional provision that earmarks the funds for a specific purpose. Like general funds, they must be appropriated annually, but they are not generally subjected to the same level of debate.

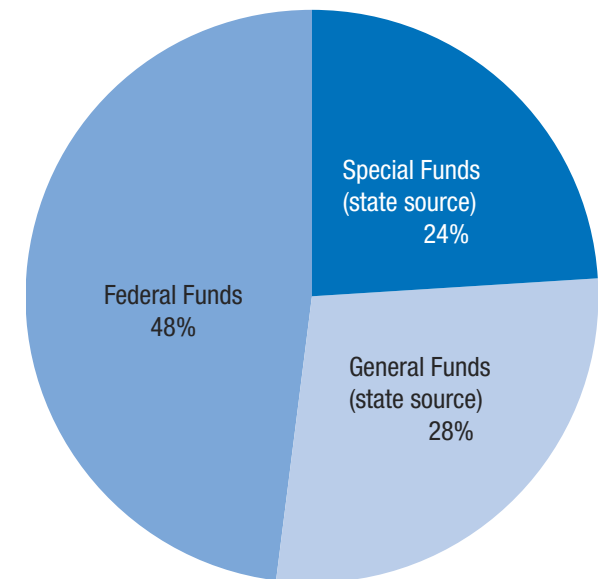
Some special funds are supported by fees, fines or assessments. Others can be funded through special taxes. For example, regulatory/licensing agencies charge licensing fees and assess fines which go to support their operation. The Medical Licensure Board and the Board of Dental Examiners are two agencies that receive funding through licensing fees. The Department of Transportation is an example of a special fund agency that derives some of its funding through a tax on fuel. Many special fund agencies, like the Medical Licensure Board, receive all of their funding from special funds.¹⁰ Some other agencies, like the Department of Human Services, receive funding from a combination of special funds, general funds, and/or federal funds.

Federal Funds

Federal funds are earmarked by the U.S. government for specific state programs. They are appropriated annually by the Mississippi Legislature, but they must be spent in keeping with federal rules. Depending on the federal rules associated with each program, the Legislature may have more or less flexibility in how the funds are spent.

Figure 1 breaks out state appropriations by fund type. The appropriations for FY 2008 included \$4.9 billion in general funds, \$4.2 billion in state-funded special funds, and \$8.3 billion in federally-funded special funds.

Figure 1:
Total Appropriations
(\$17.4 Billion) in State
and Federal Funds FY 2008



Source: Mississippi Joint Legislative Budget Committee State of Mississippi Budget Fiscal Year 2008

⁹ Mississippi Joint Legislative Budget Committee *State of Mississippi Budget Fiscal Year 2008*

¹⁰ A complete list of Special Fund Agencies can be found in the most recent enacted state budget available on the website for the Mississippi Department of Finance and Administration: <http://www.dfa.state.ms.us/fy2008appropriations.pdf>

How is the State's Budget Created?

Each year, Mississippi's legislature comes together to make decisions about how the billions of dollars in state funds will be spent in the upcoming **fiscal year**. This process is called the **budget appropriation process**. Figure 2 illustrates the steps in the timeline of the budget process.

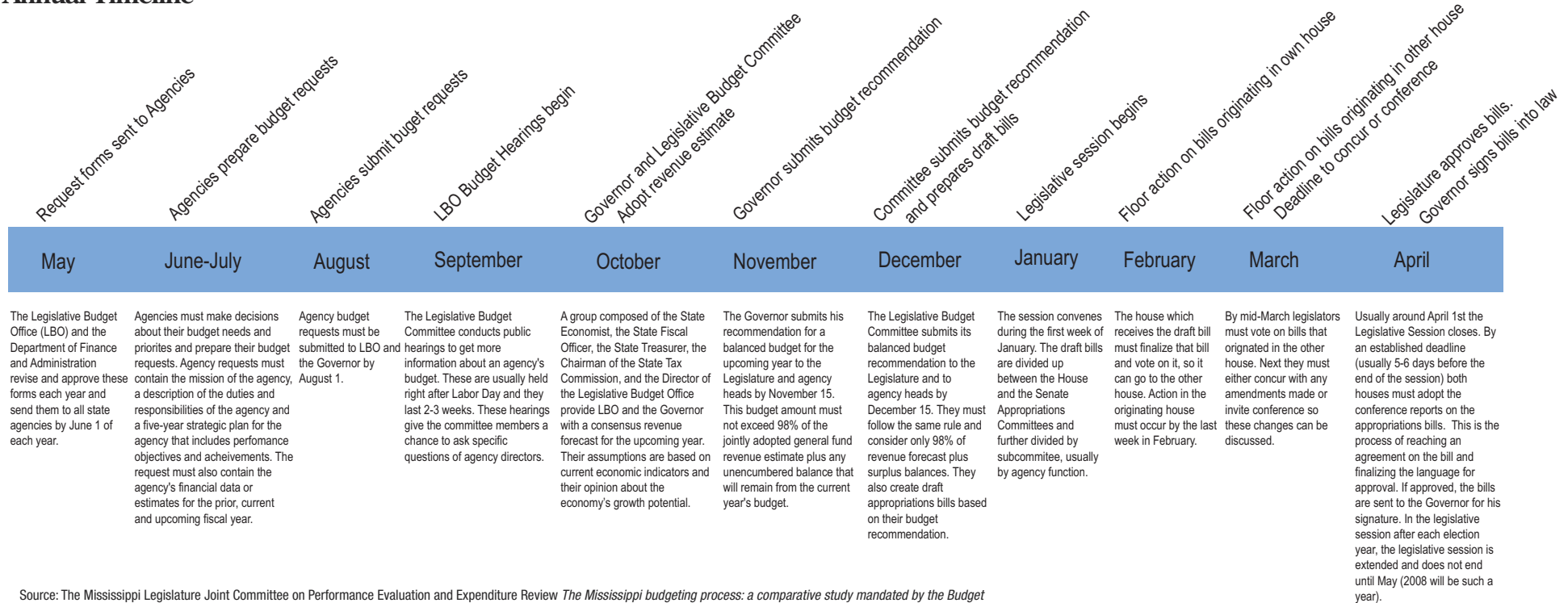
Key Terms

Fiscal Year (FY) – The yearly accounting period for which budget decisions are made. The fiscal year for the state of Mississippi extends from July 1 of one year to June 30 of the next. A fiscal year is referred to by the calendar year in which it ends. For example, FY 2007 began on July 1, 2006 and ended on June 30, 2007.

Budget Appropriation Process – The process through which the state legislature and executive branch work together to:

- Identify the state's needs for the upcoming year;
- Determine how much money is available; and
- Designate projected money available for the funding of state services for the next fiscal year.

Figure 2:
Mississippi State Budgeting Process Annual Timeline



Source: The Mississippi Legislature Joint Committee on Performance Evaluation and Expenditure Review *The Mississippi budgeting process: a comparative study mandated by the Budget Reform Act of 1992* and Department of Finance and Administration Appropriations and Budgets *Legislative Budget Office Budget Instructions/Forms Memorandum*, June 1, 2006.

The budget process begins with the state agencies. By August 1 of each year, each state agency sends a budget request to the Legislative Budget Office laying out how much it hopes to spend in the following fiscal year and on what. In September, the **Joint Legislative Budget Committee** conducts hearings open to the public to discuss all of the agency budget requests. In October, the **Revenue Estimating Committee** examines economic trends and develops an estimate of the amount of revenue the state will collect from existing sources in the next fiscal year. The committee submits the estimate for approval by the Governor and the Joint Legislative Budget Committee.

The work of the Revenue Estimating Committee underscores one of most important attributes of the state budget process: spending can only occur to the extent that funds are available.

Based on the revenue estimate, the Governor must submit a balanced budget recommendation to the Legislature by November 15. The Joint Legislative Budget Committee must respond with its own balanced budget recommendation by December 15.¹¹ This Committee's recommendation is used as the starting point for appropriations bills when the legislative session convenes in January. The House of Representatives and the Senate spend the next few

months debating, amending and voting on these budget bills. Appropriations bills in their final form must be passed by a deadline established in the legislative calendar (usually 5 to 6 days prior to the end of the legislative session).¹² Upon their passage in the Legislature, the appropriations bills are sent to the Governor for signature into law.

Throughout the process, budget recommendations and eventual decisions are published in a number of key documents that are available to the public. These documents are listed in the box on the right.

As in most other states, Mississippi's budget is required to be balanced. This means the Legislature is required by state law to pass a budget with the expectation that spending will not exceed revenues for the coming fiscal year. Specifically, proposed budgets of the Governor and the Joint Legislative Budget Committee and the final enacted budget cannot exceed 98% of projected revenues in a given year. The rule can be set aside if the law is amended, as it was for FY 2006, allowing total general fund appropriations to equal 100% of projected revenues.

If, after the legislative session is over and appropriations laws have been passed, it becomes apparent that expenditures will exceed revenues — that a deficit exists — the Governor may cut state spending to bring the current year back into balance. The State Fiscal Officer, appointed by the Governor, may cut up to 5% in any manner, but any cuts above 5% of the enacted budget must be executed as a uniform percentage of all general funds.¹³

Joint Legislative Budget Committee

The Joint Legislative Budget Committee (JLBC) is composed of 14 legislators, half from the Senate and half from the House of Representatives. The Committee is chaired either by the Lieutenant Governor or by the Speaker of the House of Representatives. The chairmanship alternates between them on an annual basis. In the Senate, the Chairman of the Senate Finance Committee, the President Pro Tempore and the Chairman of the Senate Appropriations Committee are standing members of the JLBC. The Lt. Governor names three additional members of the Senate to the Committee. In the House, the Chairman of the Ways and Means Committee and the Chairman of the Appropriations Committee are standing members. The Speaker of the House appoints four additional members of the House to the Committee. The staff of the JLBC is called the Legislative Budget Office (LBO).

Revenue Estimating Committee

Each year the Governor and the Joint Legislative Budget Committee must adopt an estimate of all the general funds that the state expects to receive from taxes and selected fees for the upcoming year. The estimates are developed by the Revenue Estimating Committee. This committee includes the State Economist, the State Fiscal Officer, the State Treasurer, the Chairman of the State Tax Commission, and the Director of the Legislative Budget Office. Their estimates are based on current economic indicators and their opinion about the economy's growth potential.

¹¹ In 2006, the Joint Legislative Budget Committee did not agree on a budget proposal for FY 2008. Subsequently, legislators made appropriations during the legislative session without the Committee's recommendations.

¹² Every fourth year, coinciding with the inauguration of an elected Governor, the regular 90-day legislative session is extended to 125 days, and the session does not end until around May 11. This is the case for the 2008 legislative session.

¹³ MISSISSIPPI CODE ANN. §27-103-211, § 27-103-139, and §27-104-13

Putting the Pieces Together on the Budget Process

- State services are funded through three primary sources: 1) General Fund dollars raised largely through state income and sales taxes; 2) State Source Special Fund dollars raised through fees and special taxes; and 3) Federal Fund dollars sent to the state and earmarked to fund specific programs.
- Through the Budget Appropriations Process, the Legislature determines how the state's money is spent. The process occurs throughout the year and includes steps that gather input through state agency budget requests and recommendations by the Office of the Governor.

- Budget requests and recommendations are informed by reports from the Revenue Estimating Committee, which forecasts the amount of revenue that the state will have available to pay for state services in the upcoming fiscal year.
- All of the budget recommendations and the final enacted budget must be balanced, and expenditures cannot exceed 98% of the state's projected revenue unless legislative action occurs.



Key Budget Documents

Agency Budget Requests: Budget Requests are prepared by each state agency for consideration by the Joint Legislative Budget Committee. Agency requests contain the mission of the agency, a description of the duties and responsibilities of the agency, and a five-year strategic plan for the agency that includes performance objectives and achievements. The request also contains the agency's financial data for the prior and current years as well as their request for the upcoming fiscal year. Depending on its complexity, an agency's budget request can range in size from around 15 pages to several hundred pages. Agency budget requests can be viewed in print by contacting the Legislative Budget Office.

Executive Budget Recommendation: Prepared by the Office of Budget and Fund Management, this book gives the Governor's recommendation for a balanced budget for the upcoming year. It usually includes a letter to the Legislature that explains the Governor's

priorities for the Budget. Although in some states the Governor's budget is the basis for the budget later enacted by the Legislature, in Mississippi the Governor's budget is advisory. The FY 2008 Governor's Budget is 19 pages long. This document is available in print, and a summary of the FY 2008 Governor's Budget is available online at Governor Barbour's website at www.governorbarbour.com.

The Legislative Budget Report: Prepared by the Joint Legislative Budget Committee, this book gives the committee's recommendation for a balanced budget for the upcoming year. It is generally used as the starting point for the appropriations bills that will be debated by the Legislature in January. For each General and Special Fund agency, it includes appropriations numbers for three fiscal years: It indicates how much was spent during the most recently completed fiscal year, how much is

appropriated for the current fiscal year, and how much the agency and the committee request for the upcoming fiscal year. This format gives the reader a good picture of each agency's recent spending history. The FY 2007 Legislative Budget Report is 682 pages long. This document is available in print from the Legislative Budget Office.

Enacted Budget Bulletin: Prepared by the Legislative Budget Office, this book is a summary of what the Legislature appropriated to each agency during the legislative session. The appropriations listed were passed by the Legislature and have been signed into law by the Governor. The FY 2008 Enacted Budget is 24 pages long. This document is available in print from the Legislative Budget Office and online on the Department of Finance and Administration website at www.dfa.state.ms.us.

CHAPTER 3 – A Detailed Look at State Spending

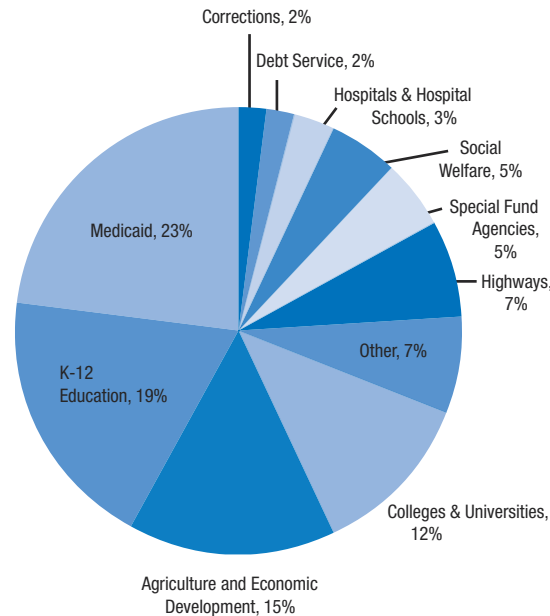


How are State Dollars Spent?

The next piece of the budget puzzle examines the question, “How does the state spend its money?” This section provides an overview of the funding decisions the Legislature has made recently and over time.

For FY 2008, Mississippi appropriated \$17.4 billion in state and federal funds. This reflects an increase of \$3.1 billion since FY 2007, largely as a result of the availability of federal funds for hurricane recovery and rebuilding. Figure 3 illustrates how this money was distributed.

Figure 3:
Total Appropriations (\$17.4 Billion) in state and federal funds approved by the Legislature FY 2008



Source: Mississippi Joint Legislative Budget Committee
State of Mississippi Budget Fiscal Year 2008

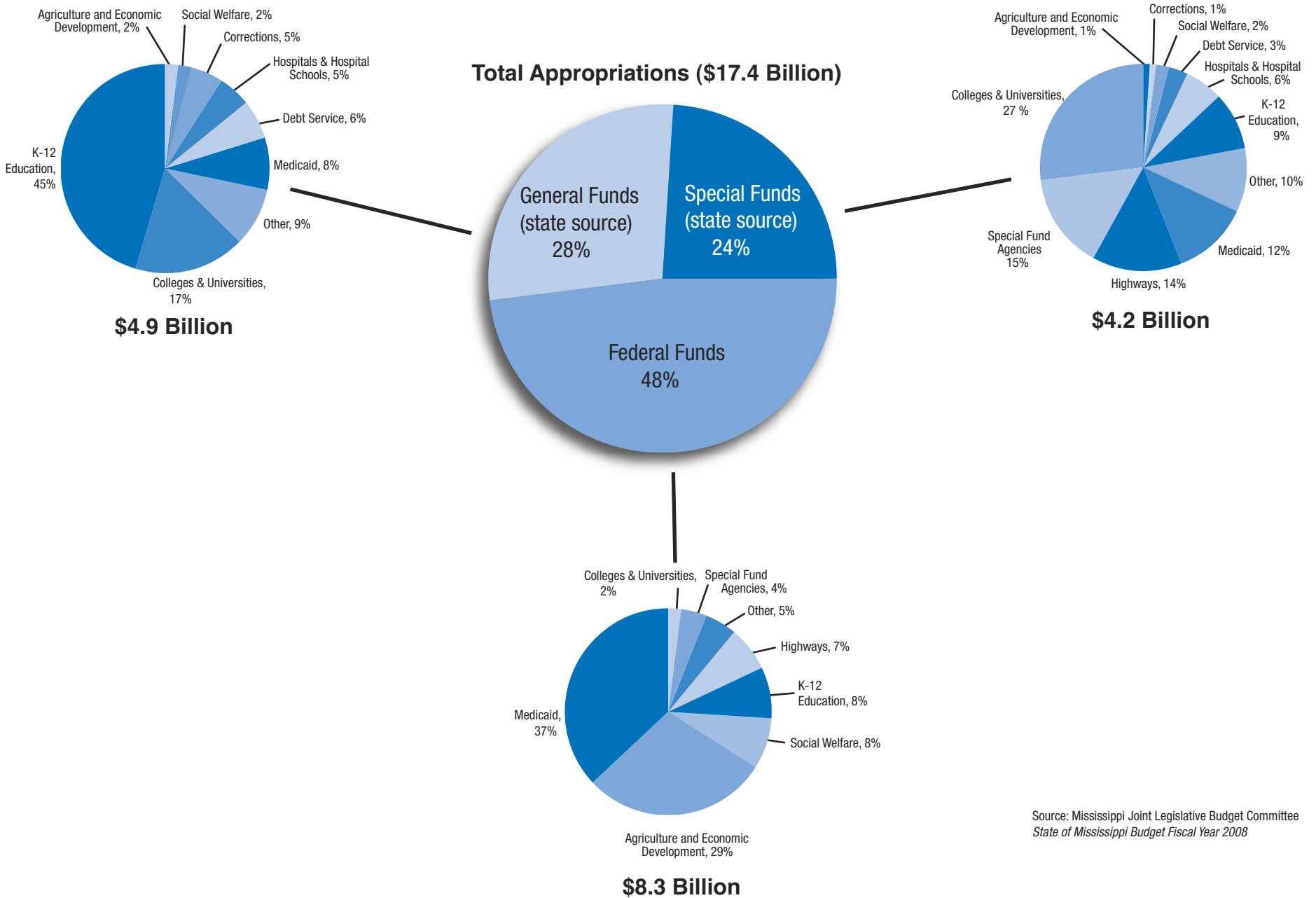
Of the \$17.4 billion appropriated, more than 75% was for Medicaid, K-12 education, colleges and universities, agriculture and economic development, and highways. Fifty-three percent (53%) of the total funding for these five largest categories came from federal sources. Over three-quarters of the appropriations for the largest category, Medicaid, came from federal sources.

It should be noted that hurricane recovery appropriations had a significant effect on the FY 2008 budget. For example, Agriculture and Economic Development is not usually one of the largest appropriations categories; however, it accounts for 15% of the total appropriations for FY 2008. These appropriations were largely funded with federal dollars through the Mississippi Development Authority — the agency responsible for administering the federal funds for Hurricane Katrina recovery. As a comparison, Agriculture and Economic Development appropriations for FY 2007 only accounted for 2% of total appropriations.

As noted in Chapter 2, the state budget comprises three types of funds: general funds, special funds, and federal funds, with federal-source funds being the largest of the three (see Figure 1). The services and programs shown in Figure 3 are funded with different mixtures of the three types of funds, with some paid for entirely by General Funds and others funded primarily by Special Funds or Federal Funds. Figure 4 shows the breakdown of general fund, federal fund, and other state-source special fund appropriations for FY 2008.

As Figure 4 indicates, Public Education and Higher Education, combined, will receive over half of every general fund dollar and only 10 cents of every federal fund dollar. In contrast, Medicaid will receive eight cents of every general fund dollar and 37 cents of every federal fund dollar.

**Figure 4:
Appropriations by Fund Type FY 2008**



Source: Mississippi Joint Legislative Budget Committee
State of Mississippi Budget Fiscal Year 2008



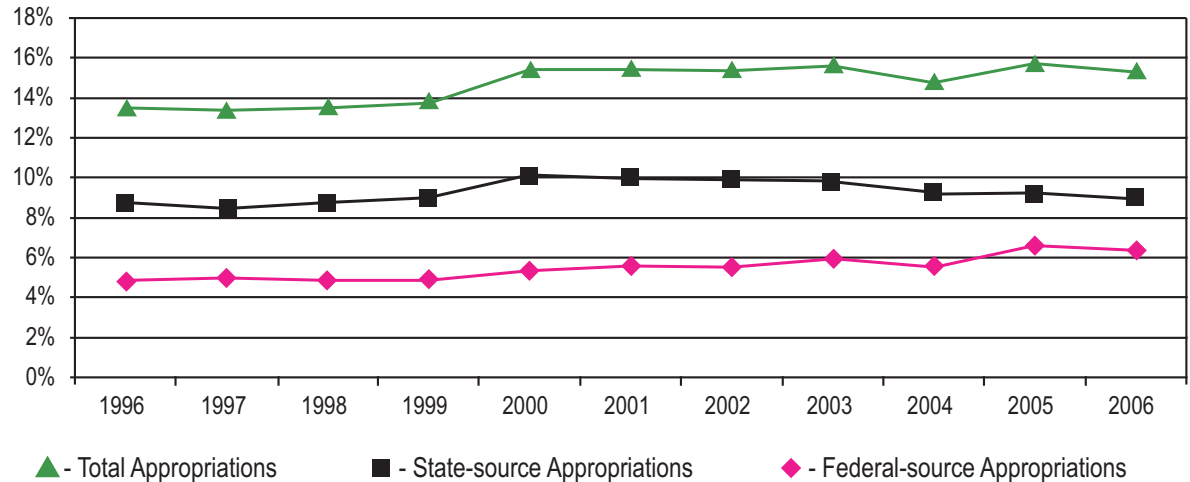
How has State Spending Changed over Time?

There are many different ways to look at changes in state spending. Going back to our analogy of family spending patterns, a family may incur more expenses as children are born, and as elderly parents age. Likewise, as the prices of gas, groceries and health care increase, a family must find ways to pay for increases in the costs of goods and services. Similarly, the state's spending requirements change as it adds population, and as the prices it pays for things change.

One way to take these changes into account is to adjust spending for inflation; that is, to take into consideration the fact that prices increase every year on most everything the state buys — both goods (like schoolbooks) and services (like health care). Because of inflation, a dollar buys less today than it did in 2000. Adjusting for inflation controls for these changes, so the amount of goods and services purchased this year can be compared with the amount purchased in other years.

Adjusting for inflation is important, but it leaves out other important contexts for state spending, such as population changes and the amount of money people in the state are earning. Another method captures these factors, and that is to look at state spending as a percentage of the **State Gross Domestic Product (GDP)**. The State GDP is a measure of the state's total economy, and therefore is an important indicator of how much the state can afford to spend on public priorities. Figure 5 shows the trends in total, federal-source, and state-source appropriations as a percentage of State GDP.

Figure 5:
Total Appropriations, Federal and State Appropriations as a Share of the State's Economy (FY 1996-FY 2006)



Source: Mississippi Joint Legislative Budget Committee *State of Mississippi Budget (1996-2006) Schedule IV* and Marianne Hill, Mississippi Institutions of Higher Learning University Research Center, *Mississippi Economic Review and Outlook*, June 2007 gross state product data

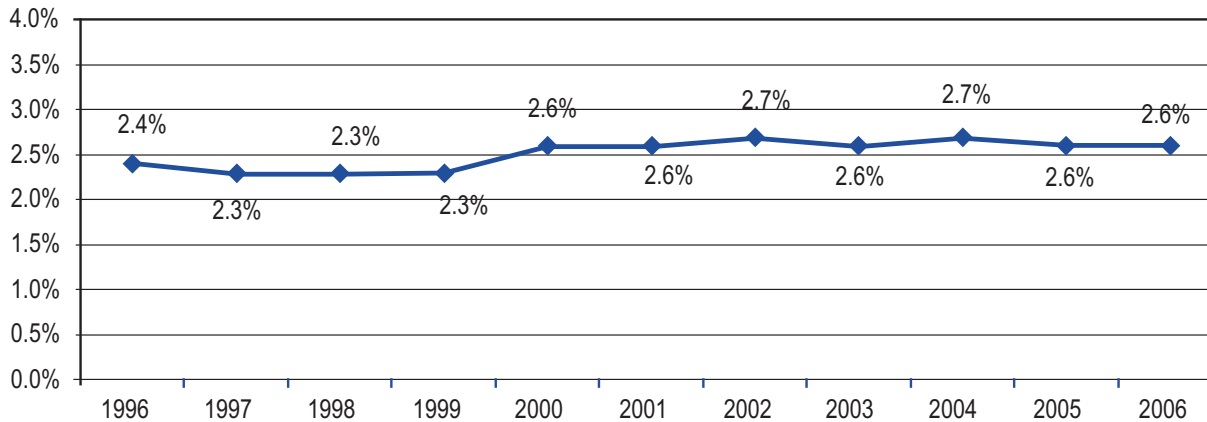
Figure 5 shows that between 1996 and 2006, state-source spending as a share of the state's economy held relatively steady, peaking in 2000 and declining slightly through 2006. In 2000, state-source spending represented 10.1% of the State Gross Domestic Product. By 2006, these appropriations had fallen to 9% of the state GDP.

While state-source spending held relatively steady as a share of the Mississippi economy over the last several years, the state benefited from increases in federal funds. Federal appropriations as a share of the state's economy rose from 4.9% in 1996 to 6.4% in 2006. This growth was primarily the result of increased federal spending on health care, transportation and social services. Because of the increase in federal funds, total state spending increased as a share of the state's economy — from 13.5% in 1996 to 15.4% in 2006 — even as spending from state sources held relatively steady.

Key Terms

State Gross Domestic Product (GDP) – State Gross Domestic Product is a measure of the total income produced in the state in a given year, including salaries, dividends, and interest. As a measure of the state's income, State GDP is useful for determining how much the state can afford to spend on public priorities.

**Figure 6:
Public Education State-source Appropriations as a Share of the State's
Economy (FY 1996-FY 2006)**



Source: Mississippi Joint Legislative Budget Committee *State of Mississippi Budget (1996-2006) Schedule IV* and Marianne Hill, Mississippi Institutions of Higher Learning University Research Center, *Mississippi Economic Review and Outlook*, June 2007 gross state product data

Putting the Pieces Together on state spending

- * For FY 2008, the Mississippi State Legislature appropriated over \$17 billion. The appropriations included state and federal funds.
- * The biggest overall expenditure was Medicaid, which was primarily funded with earmarked federal dollars. The largest general fund appropriations were made for education, both K-12 and colleges and universities.
- * General Fund spending, as a percentage of State GDP, has been relatively stable, suggesting that increases or decreases in spending are in line with the growth of the state's economy.

What about Large Budget Items?

As discussed above, a meaningful way to look at changes in spending over time is as a percentage of State GDP. An analysis of large budget items, including public education, higher education, and corrections, shows that spending in these areas has remained relatively steady over the past decade. As the largest general fund item, public education expenditures serve as a good example of this trend. Public education spending has stayed fairly constant as a share of the state's economy (Figure 6).



CHAPTER 4 –

A Detailed Look at State Revenue



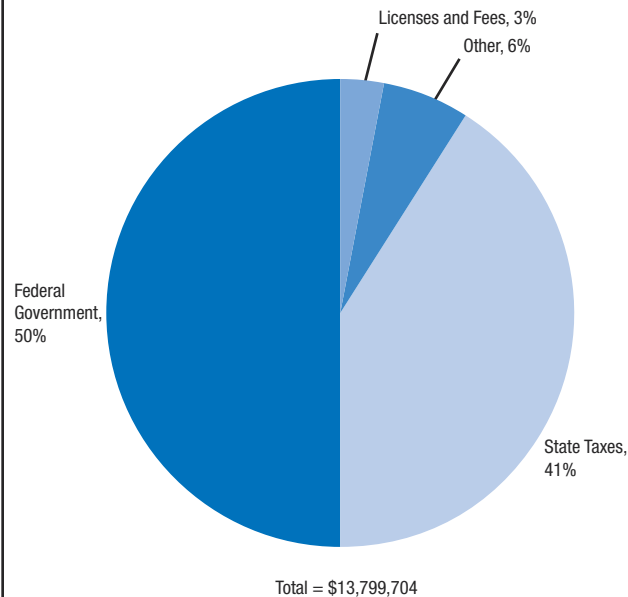
From Where Does the State Get its Money?

After hearing about how the state spends its money, a natural question is, “How does the state pay for all of its programs and services?” In order to make government work, the state collects **revenue** from residents and businesses in the form of taxes and fees. The state also receives money from the federal government to assist in providing certain government services (Figure 7).

Key Terms

Revenue – The state’s income from any source, including tax collections, fees, and intergovernmental grants.

Figure 7:
State of Mississippi Governmental Fund Revenues by Source, FY 2006



Source: *Mississippi Comprehensive Annual Financial Report FY 2006*, p. 158

In FY 2006, the state collected \$13.8 billion¹⁴ in revenue from residents, businesses and the federal government.¹⁵ Of each dollar collected by the state of Mississippi, 41 cents came from state taxes, 50 cents came from the federal government and nine cents came from licenses, fees, interest, court settlements, and other sources.

State Taxes

The state collects taxes from individuals and businesses within the state. State taxes include:

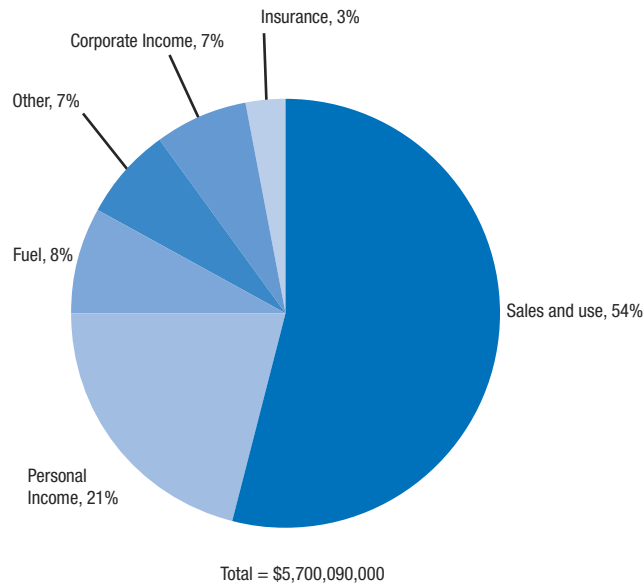
- Income taxes, which are a percentage of individual and business income;
- Sales and use taxes, which are a percentage of the price of goods and services purchased in the state; and
- Special taxes on certain businesses, like casinos, and certain goods, like gasoline.

In FY 2006, Mississippi collected \$5,700,090,000 in state taxes. Figure 8 shows Mississippi’s tax revenue collections by source in FY 2006.

¹⁴ Please note that the total revenue figure for FY 2006 (\$13.8B) is different from the \$17.4B total appropriations in FY 2008 because they refer to different years. Appropriations data is available sooner than revenue data for a fiscal year because appropriations are made in advance of the fiscal year, while revenue data is not compiled until after the close of a fiscal year. While the raw number of appropriations usually goes up every year, the large increase between FY 2006 and FY 2008 is largely due to the availability of federal funds for hurricane recovery and rebuilding.

¹⁵ This amount only includes the State’s governmental funds, such as the general fund, the health care fund accounts, the capital projects fund accounts, special revenue funds, debt service funds, and some other permanent funds. It does not include component units such as Universities. Some of the other data provided on tax revenue for individual taxes is from the State Tax Commission’s Annual Report and shows all tax collection.

**Figure 8:
State Tax Revenue by Source FY 2006**



Source: *Mississippi Comprehensive Annual Financial Report FY 2006*, p. 158

As shown in the chart, sales and use taxes made up the largest portion of state tax revenue in FY 2006 at 54%. The second largest revenue stream was the personal income tax, which made up 21% of state revenues. The corporate income tax made up only 7% of state tax revenue.

Sales Tax

Mississippi generated most of its state tax revenue, \$3,074,831,000 (54%) from the sales and use taxes.¹⁶ According to an analysis of U.S. Census data, Mississippi ranked 7th in the country in the amount of general sales taxes paid per resident in FY 2006 (\$1,047).¹⁷

Traditionally, sales taxes are charged on the purchase of goods. Mississippi taxes most goods at a rate of 7%. Mississippi's sales tax on goods includes all retail purchases of tangible personal property including, but not limited to groceries, clothes, toiletries, and over-the-counter medications. The state also charges a 5% sales tax on automobiles.¹⁸

Mississippi also taxes some services at the rate of 7%. For example, the installation of air conditioning systems and electrical work are taxable services. However, some services are not taxed. Some services that are not taxed include many professional services, such as legal services, accounting services and other services like dry cleaning and massage therapy.

Of the \$2.8 billion in sales taxes collected in FY 2006, about half of the collections came from taxing food, vehicles, and general merchandise (including clothes).¹⁹ The tax on food is notable because Mississippi charges one of the highest sales tax rates on groceries in the nation. Only Mississippi and Alabama still extend their full sales tax rate to groceries. Other states with a sales tax on groceries provide a rebate or credit that offsets some of the sales taxes paid on groceries by some residents.²⁰ Mississippi — as required of all states by federal law — does exempt food purchases made with food stamps and through the Women, Infant, and Children's (WIC) Program from sales tax.

Personal Income Taxes

In FY 2006, the personal income tax was the state's second largest source of tax revenue. Mississippi collected 21% of its tax revenues, or \$1,213,733,000, from individual income taxes.²¹ Of the 43 states that have an income tax, Mississippi ranked 41st in the amount of income taxes paid per person (\$431), according to an analysis of FY 2006 Census data.²² Mississippi's income tax is relatively flat, meaning that most taxpayers pay a similar effective tax rate. There are three tax brackets — 3%, 4%, and 5% — and everyone with more than \$10,000 in taxable income pays at the top (5%) rate.²³ Taxable income is total income minus a number of exemptions and deductions, which add up to about \$20,000 for a typical family of four, but can be more if the taxpayer itemizes deductions.²⁴

Corporate Income Taxes

The corporate income tax is a tax on business profits. Only about 7% of the state's revenue in FY 2006 came from taxing businesses through the corporate income tax. Corporate income taxes work in much the same way as the personal income tax, with brackets of 3%, 4%, and 5%.²⁵

A corporation's income tax liability may be reduced by one of the state's many corporate tax credits. Tax credits lower the tax owed by the corporation by the amount of the tax credit. In Mississippi, tax credits are provided to corporations for a wide variety of actions, including creating new jobs, providing child/dependent care for employees, and producing motion pictures in the state.²⁶

¹⁶ Use tax is similar to sales tax, but applies to purchases on which sales taxes were either not paid or were paid at a lower rate than Mississippi sales tax law requires. Often, this law applies when the purchase of an item, such as an automobile, is made in another state. Use tax rates are the same as those applicable under the sales tax law, but the taxpayer receives credit for any sales tax already paid on the item. The State collected \$280,459,459 in use taxes in 2006.

¹⁷ MEPC Analysis of data from the U.S. Census Bureau
¹⁸ MISSISSIPPI CODE ANN. §27-65-17

¹⁹ *Mississippi State Tax Commission Annual Report FY 2006*, pp. 82-84

²⁰ Center for Budget and Policy Priorities *Which States Tax The Sale of Food for Home Consumption in 2007?*, February 23, 2007

²¹ *Mississippi Comprehensive Annual Financial Report FY 2006*, p. 158

²² MEPC Analysis of data from the U.S. Census Bureau

²³ MISSISSIPPI CODE ANN. §27-7-5

²⁴ MISSISSIPPI CODE ANN. §27-7-21, §27-7-17

²⁵ MISSISSIPPI CODE ANN. §27-7-5

²⁶ Mississippi State Tax Commission Tax Incentives for Economic Development, 2004

Mississippi also charges a franchise tax on businesses operating in the state at a rate of \$2.50 per \$1,000 of the value of resources invested in the State.²⁷ The minimum franchise tax to be paid by Mississippi corporations each year is \$25. Corporations pay the franchise tax on top of their corporate income tax liability.

In FY 2006, Mississippi collected \$354,751,599 in corporate income and franchise taxes after granting \$70,020,715 in tax credits to corporations.²⁸ The collections in FY 2006 amounted to \$109 per capita, for a ranking of 39th out of the 47 states with corporate income tax collections.²⁹

Other State Taxes

The remaining 18% of the state's tax revenue came from a number of other taxes including cigarette taxes, taxes on gaming establishments, and taxes on fuel and insurance.³⁰

Local Taxes

Like the state, counties and municipalities levy taxes to pay for the services they provide. These taxes include property taxes, special sales taxes, and other taxes such as local utility taxes. The largest of these is the property tax, which is paid by individuals, businesses, and public utilities on the property they own, including real estate, automobiles, and other personal property.

Property taxes are the largest source of tax revenue for Mississippi's counties and municipalities. On average, 93.4% of local tax revenue is collected from property taxes.³¹ This revenue is used to fund most of the public services that residents rely on, including public education, police and fire services, and garbage collection. About 40% of the taxes collected on a county level are used to fund county schools; an additional one-third of the tax revenue is used to fund the county general fund, which pays for county administration; and the remaining revenue pays for services such as fire protection and garbage collection.³²

In Mississippi, both **real property** and **personal property** are taxed. Real property encompasses all real estate, and personal property includes automobiles, mobile homes, furniture, machinery and equipment, and inventories.

Key Terms

Real Property – property, such as land and buildings, that cannot be moved

Personal Property – property, such as automobiles and mobile homes, that can be moved

Ad Valorem Taxes – tax based on the value of real or personal property

Other Revenue Sources

Federal Funds

As shown in Figure 7, 50%, or \$6.8 billion, of state revenues came from the federal government in FY 2006. The federal government provides money to states to help pay for specific programs. Often, the state is required to pay a portion of the program costs by matching federal dollars. For example, in FY 2006, the state's federal Medicaid match rate was 76%, meaning that for each dollar of Medicaid spending, 24 cents were paid by the state, and 76 cents were paid by the federal government.³³

Over the last several years, Mississippi has experienced an increase in the share of total state revenues it receives from the federal government (Figure 9). Federal Medicaid payments to cover the rising cost of health care account for a large portion of the increase.



²⁷ MISSISSIPPI CODE ANN. §27-13-5

²⁸ *Mississippi State Tax Commission Annual Report FY 2006*, pp. 51-56

²⁹ MEPC Analysis of data from the U.S. Census Bureau

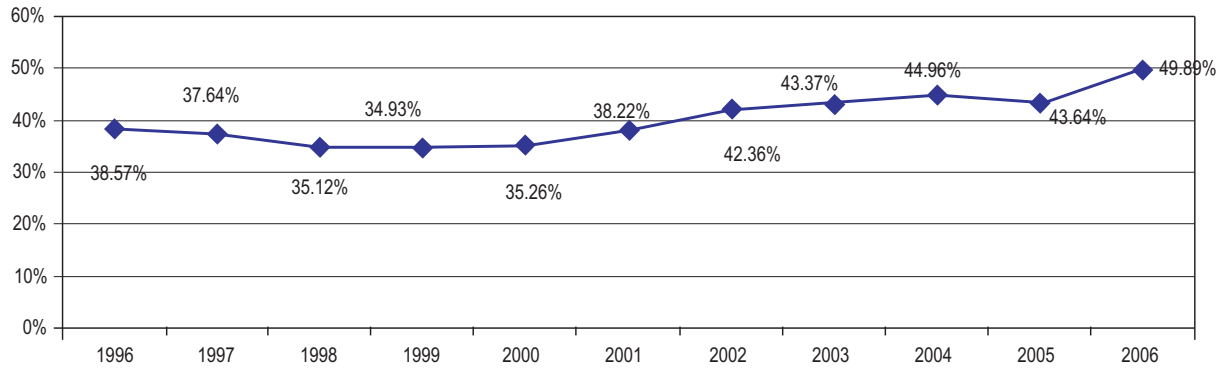
³⁰ *Mississippi State Tax Commission Annual Report FY 2006*

³¹ U.S. Census Bureau, *State and Local Government Finances: 2004-05*, www.census.gov

³² Mississippi State Tax Commission *2005-2006 County Millage Rates*

³³ Georgetown University Health Policy Institute Center for Children and Families *FMAP rates 2006*

**Figure 9:
Federal Revenues as a Share of Total Governmental Fund Revenues FY 1996 – FY 2006**



Source: *Mississippi Comprehensive Annual Financial Report*, FY 2003, 2005, 2006.

Fees

Fees are funds collected from users of a particular government service. For instance, the Department of Motor Vehicles charges a fee for a driver's license. The state's public universities charge tuition. Fees are generally set up so that those who don't use a service do not have to pay for that service. In practice, however, many programs are paid for partially by fees and are subsidized with taxes as well.

In FY 2006, the state received \$448,482,000 in licenses, fees, and permits, and \$279,899,000 in charges for sales and services of governmental funds. Charges for sales and services include revenues such as funds collected through the wholesale sales of alcoholic beverages and the sale of state assets like real estate.³⁴

Putting the Pieces Together on State Revenue

- In FY 2006, Mississippi collected \$13.8 billion in revenue. Most of the revenue came from state taxes and federal funds.
- The two primary sources of state tax revenue are the sales tax and the income tax. Mississippi ranks very high relative to other states in the amount of money collected per person through the sales tax. Conversely, Mississippi ranks very low in the amount of money collected per person through the income tax.
- Mississippi receives a large share of its annual revenue from federal funds. Over the years, the amount of federal funds as a share of total state revenue has increased.



³⁴ Mississippi Department of Finance and Administration Staff.

Evaluating Mississippi's Tax System



How Does One Evaluate a Tax System?

There are a number of factors used to evaluate a tax system. While opinions on what qualifies as a good tax system differ, there is general agreement that some of the most important factors include adequacy, fairness, stability, and transparency.³⁵

Adequacy

A tax system is considered adequate if it collects enough revenue to pay for the services required by residents and policy makers.

One threat to the adequacy of a tax system is a **structural deficit**. In states with a structural deficit, revenues do not grow at the same rate as the costs of providing government services. As noted earlier, providing services becomes more expensive each year as the costs of goods and labor increase. If revenues do not keep up with these increased costs, the state must either raise taxes or cut services. In a state without a structural deficit, the tax system will collect sufficient revenue each year to cover the increased costs without raising tax rates.

Fairness

There are two main areas of thought on tax fairness, and both can be incorporated in a good tax system. The first area of thought, which is most commonly considered when evaluating tax fairness, is the “ability to pay principle.” This principle suggests that persons with higher incomes, or greater ability to pay, should pay more in taxes than those with lower incomes. Based on their adherence to this principle, taxes can be categorized into three types:

- **Progressive:** A tax system is progressive if persons with higher incomes pay a greater percentage of their income in taxes than those with lower incomes. Most income taxes, including the federal income tax, are designed to be progressive.
- **Proportional:** A tax system is proportional if all persons, regardless of income level, pay the same percentage of their income in taxes.
- **Regressive:** A tax system is regressive if persons with lower incomes pay a higher percentage of their income in taxes than those with higher incomes. Sales taxes are generally regressive because families with lower incomes tend to spend a larger fraction of their income on taxed goods than do higher-income families.

Key Terms

Structural Deficit – A situation in which a government’s tax structure is not designed to collect enough revenue to pay for services as costs increase.

The second area of thought, the “benefit principle,” maintains that persons who benefit more from a service should pay more for that service than those who benefit less. This principle is often the justification for establishing special taxes or charging fees for government services. For instance, highway maintenance is paid for in part by a petroleum tax. As a result, persons who drive on the roads are paying more for highway maintenance than others. However, many programs are only partially paid for by fees, because they provide value to the public beyond those who benefit directly. For example, the Wildlife, Fisheries and Park Department receives fees from hunting and fishing licenses and from visitors to state parks, but it also receives general funds because even those who do not visit state parks, or hunt and fish, benefit from the Department’s work.

Stability

A stable tax system provides a steady revenue stream as the economy rises and falls. A tax system that is sensitive to economic downturns results in less tax revenue when government services are often needed most. Likewise, an unstable tax system may result in a surplus during times of economic prosperity.

Transparency

The transparency of a tax system indicates whether or not information about the tax system is easy to obtain. Available information should include who and what is taxed, the process for making tax decisions, and how the funds collected are spent. Some states with high transparency use tools like fiscal notes and tax incidence analysis. Fiscal notes provide an estimate of the revenues gained or lost for a proposed change in law. Tax incidence analysis provides an estimate of how different income groups are affected by a tax or proposed tax change.

³⁵ Institute on Taxation and Economic Policy *Guide to Fair State and Local Taxes*, February 2005; Tax Foundation *Ten Principles of Sound Tax Policy*, and the National Conference on State Legislatures *Principles of a High-Quality State Revenue System*, Fourth edition, June 2001

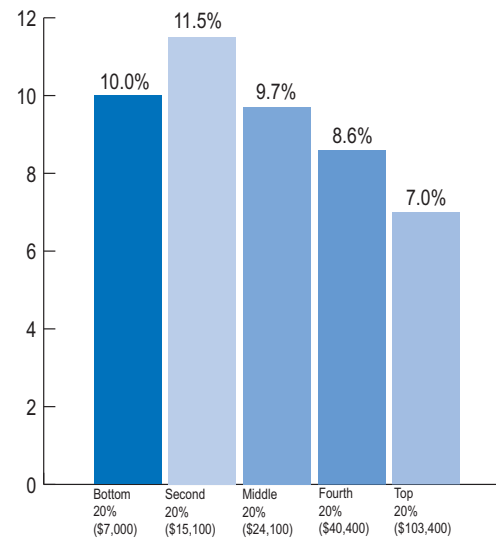
Evaluating Mississippi's Taxes

Mississippi's bundle of taxes has some progressive elements and some regressive elements. As a whole, Mississippi's state tax policies are regressive: the top 20% of income earners pay the lowest percentage of their income towards state and local taxes, while the bottom 40% pay the highest percentage of their income towards state and local taxes (Figure 10).

An analysis of Mississippi's sales and income taxes illustrates some of the strengths and weaknesses of Mississippi's tax system.

Figure 10:
Total taxes paid as a percentage of income by income group - 2002

(Average income is in parentheses)



Source: MEPC Analysis of data from the Institute for Taxation and Economic Policy.
Note: Total taxes paid takes into account the amount of state and local taxes paid that can be deducted on a filer's federal income tax form, if the taxpayer itemizes

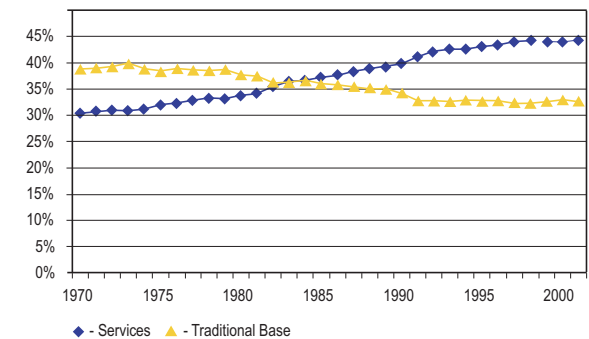
Mississippi Sales Tax

As seen in Figure 8, Mississippi sales and use tax represents over half of state tax revenues. States with a strong emphasis on a sales tax tend to have more regressive tax systems, because people with low incomes pay a higher proportion of their income on taxed items — for example, groceries and clothing — than people with high incomes. Sales taxes can be made more or less regressive depending on what goods or services are taxed. Mississippi's sales tax is more regressive than other states' because Mississippi taxes food at the full 7%. With Arkansas' reduction of sales tax on groceries in July of 2007, Mississippi is now one of only two states to fully tax food without any offsets.³⁶

According to an analysis of U.S. Census data, Mississippi ranks 7th in the country in the amount of general sales taxes (\$1,047) paid per resident of the state.³⁷

From an adequacy and stability standpoint, taxing services could expand the tax base and allow tax revenues to keep up with the growth of the economy. From 1970 to 2001, the purchase of services increased from 31% to 44% of all household purchases nationally.³⁸ During the same period, goods traditionally subject to the sales tax fell from 39% to 33% of household purchases (Figure 11). As a result of this shift in buying patterns, revenue from sales taxes on goods is not keeping up with the growth in sales overall.

Figure 11:
Household Consumption of Items Composing Traditional State Sales Tax Base vs. Household Consumption of Services 1970-2001



Source: Center on Budget and Policy Priorities

³⁶ Center on Budget and Policy Priorities *Which States Tax The Sale Of Food For Home Consumption In 2007?*, February 23, 2007

³⁷ MEPC Analysis of data from the U.S. Census Bureau

³⁸ Center on Budget and Policy Priorities *Expanding Sales Taxation of Services: Options and Issues*, June 19, 2003

Mississippi Personal Income Tax

Mississippi's individual income tax is progressive, but only slightly so. The top tax rate of 5% starts at \$10,000 of taxable income, or \$29,600 of gross income for a family of four. Thus a family of four earning \$30,000 pays the same marginal tax rate as a family of four earning \$250,000. In essence, Mississippi's income tax operates more like a proportional, or flat, tax than a progressive tax.

Additionally, since 2005, Mississippi has taxed the income of families below the poverty line (Figure 12). The poverty line is adjusted for inflation. Each year, the poverty level for a family of four increases. Whereas the poverty line for a family of four was \$19,307 in 2004, the poverty line rose – along with the costs of many other things, like food and gas – to \$20,615 in 2006. During the same period, Mississippi's tax threshold – the amount of income on which Mississippians start

paying income taxes – remained the same at \$19,600. Without adjustment, the number of families in poverty subject to income taxes will increase each year, as the federal poverty level increases, but the tax threshold remains the same.

Mississippi's Corporate Income Tax

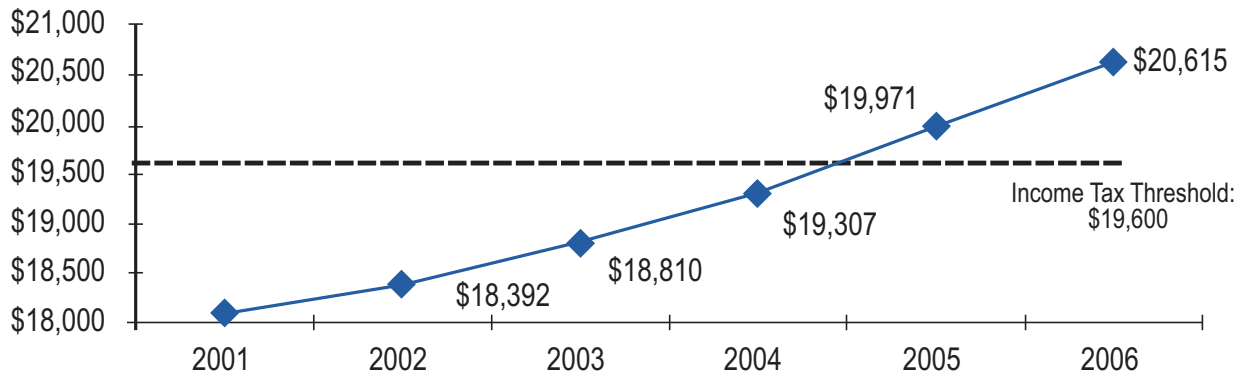
Mississippi currently offers a range of corporate tax incentives to stimulate economic development. In recent years, the state has taken some positive steps towards measuring the effectiveness of these incentives. For example, the state provides a quarterly report on the Advantage Jobs Initiative (AJI) which outlines the total jobs assisted or created by economic development projects receiving the AJI subsidies. On the other hand, there are some programs where there are no good channels to gather information on the programs' effectiveness. For example, the Jobs Tax Credit provides a credit of up to 10% of a company's

payroll against corporate income taxes.³⁹ The Annual Tax Expenditure Report estimates that employers will claim credits of about \$22,000,000 against their corporate income tax in 2007.⁴⁰ However, there is no way to answer questions about the number of jobs that are created through the credit, because of the way it is reported through the tax filing system. A system of making the incentive impact information publicly available and easily accessible would increase accountability to ensure the overall effectiveness of the incentive program.

Putting the Pieces Together – Evaluating Mississippi's Tax System

- While Mississippi's tax system has some progressive elements and some regressive elements, it is regressive overall because of its heavy reliance on the sales tax.
- The Mississippi sales tax is regressive. People with low incomes pay a higher proportion of their income towards the tax than people with high incomes. Mississippi's sales tax is especially regressive because it fully taxes groceries – an expenditure that low-income working families cannot avoid making.
- The income tax is structured to be progressive, but a large proportion of taxpayers pay the tax at the top rate. Additionally, in 2006, some families in poverty will pay income taxes due to tax thresholds that have not been updated in several years.
- Taken together, the bundle of state tax policies is not as fair as it might be: the top 20% of income earners pay the lowest percentage of their income towards state taxes, while the bottom 40% pay the highest percentage of their income towards state taxes.

Figure 12:
State Income Tax Threshold and Federal Poverty Line for a Family of Four (2001-2006)



Source: Center on Budget and Policy Priorities *The Impact of State Income Taxes on Low-Income Families in 2006*, March 27, 2007



³⁹ Information about Mississippi Development Authority Tax Credits/Exemptions is available at <http://www.mississippi.org/content.aspx?url=/page/3350&>

⁴⁰ Institute of Higher Learning Center for Policy Research and Planning *2006 Tax Expenditure Report*

CHAPTER 6 –

Putting the Pieces Together: How Mississippians Can Get Involved



Although the Legislature and the Governor make spending decisions, taxpaying residents also have an important role in the budget process. Residents have the responsibility to ensure that the state budget meets the collective needs and reflects the collective values of all the state's people. There are many ways to track and influence the budget-making process. Below are several examples of ways to get involved.

Step #1 – Keep Current

The most basic way that one can be involved is to know what is going on. Reading the newspaper and watching the news are excellent first steps. In addition to the stories that run on the front page and local sections, the Sunday paper often includes editorials that comment on tax and budget issues – especially on hot topics.

Step #2 – Enhance your Knowledge

If a newspaper article or TV news story piques your interest, there are several good sources for additional information. The Center for Policy Research and Planning at the Mississippi Institutions of Higher Learning publishes the *Annual Tax Expenditure Report*, which includes information on how much the state spends on corporate tax credits. The Center also produces a publication called the *Mississippi Economic Outlook and Review*. Likewise, the Mississippi Economic Policy Center (MEPC) conducts budget and tax analyses and posts them online at www.mepconline.org. You can sign up for e-mail updates on the MEPC website as well.

Step #3 – Engage Others

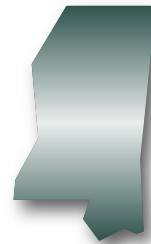
The easiest way to get involved is to contact a nonprofit organization that is already working on an issue of interest. Many nonprofit organizations have an understanding of the budget process and can tell you how to get involved – from writing a letter to a legislator to meeting face-to-face with government officials.

Nonprofit advocacy organizations can also help keep you updated on key people and events influencing the legislative process. For example, nonprofit organizations often know which legislators are important to contact on issues you care about. The organizations can also alert you about special hearings or provide summaries of the hearings if you are unable to attend.

Looking Ahead

If you've made it this far, we hope that Mississippi's Budget and Tax systems have become a little less puzzling to you. Budget decisions directly influence the quality of education that our children receive, the condition of the roads that we travel, the safety of our communities and the level of trust we can place in professionals such as doctors, dentists, pharmacists and nurses. Of course, each of these services – education, road maintenance and public health and safety – has a price tag and must be paid for through taxes or fees. Strong fiscal systems are needed to ensure that the funds are available – in a good economy or in a slow economy – to cover the costs of the services that Mississippi residents depend on every day. It is important to know how the system works to ensure that it works efficiently and effectively.





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