Special Report / Viewpoint

The Mississippi Budget: An Overview of Selected Revenue and Expenditure Patterns

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For tables 9 through 17, and the charts and figures, contact the authors.

Executive Summary

The current regressive tax system in Mississippi must change before Mississippi can adequately meet current and projected revenue needs. Mississippi families making $19,000 or less are estimated to be paying roughly 20 percent of the state and local tax revenues paid by families. Families in the lowest two income quintiles are estimated to pay 10 and 11.5 percent (respectively) of family income in taxes, while a family in the highest 1 percent pays only 6.9 percent of its income in state and local taxes.

The primary reasons for the regressive structure of state taxes are a highly regressive state sales tax and a very mildly progressive personal income tax.

Both in real dollars and as a percentage of total Tax Commission revenues, statewide corporate income taxes have steadily declined in Mississippi and other states, even in times when federal corporate income tax rates have risen.

There is little information about the effects that various exemptions from state taxes have on state revenue, and this issue should be explored in depth.

The need for additional state revenue comes not just from depressed economic conditions, but also from both devolution of federal programs to state levels and dramatic increases in health care and similar costs to the state.

Many programs are not adequately funded, and as conditions worsen, the state is faced with either reducing services or not adequately funding programs with money needed to meet matching-funds requests.

It is recommended the state of Mississippi take several actions to meet current and projected revenue needs:

(1) enact measures to make the personal income tax more progressive;

(2) investigate the decline in corporate income tax to understand why revenue losses have occurred, and if possible remedy the situation; and

(3) examine the cost of state tax exemptions, deductions, and tax credits to determine their impact on the overall tax system.

Introduction

"Taxes are the price we pay for civilization."

Oliver Wendell Holmes Jr.

"The art of taxation consists in so plucking the goose as to obtain the largest amount of feathers with the least possible amount of hissing."

J.B. Colbert

Mississippi is currently facing a shortage in revenue needed to meet current and future state expenditures. Before this situation can be addressed, the nature of Mississippi's finances and overall tax structure must be understood. This study examines Mississippi's budget over the period from 1998 through 2002 to:

(1) provide a historical analysis of both budget categories and benefit incidence of each major type of state expenditure in statistical and graphical forms;

(2) provide an analysis of budget categories by the source of revenue and analyze changes in the regressivity or progressivity of the state's tax structure over time; and

(3) provide an analysis of current budget revenue sources and exemptions with an emphasis on explicit and implicit tax incidence.

This study is organized into four sections. Section I provides background, fiscal, and revenue information, as well as an overview of how other states are dealing with the current economic downturn. Section II examines tax revenues in Mississippi between 1998 and 2002, including a discussion of tax burdens and distribution. Information on past expenditure trends and the implied incidence of benefits from these expenditures is presented in Section III, while Section IV draws conclusions and presents recommendations regarding costs, benefits, and the overall incidence of both revenues and expenditures.

Table 1
Mississippi State General Fund (in millions)

Fiscal Year	Beginning Balance	Revenues	Adjustments	Total Resources	Expenditures	Adjustments	Ending Balance	Budget Stabilization Fund
2001	21	3,444	62	3,527	3,613	-107	21	179
2002	16	3,369	37	3,422	3,584	-167	5	0
2003	2	3,457	0	3,459	3,387	0	72	0

Notes to table:

Fiscal 2001 "Revenue adjustments include a $50 million transfer from the rainy day fund and $12.3 million in state-source special fund budget cuts that were deposited in the general fund. Expenditure adjustments reflect $106.9 million in general fund budget cuts."

Fiscal 2002 "Revenue adjustments include a $50 million transfer from the rainy day fund to the general fund less a $32.2 million transfer from the general fund to the Budget Contingency Fund. Expenditure adjustments reflect $150.6 million in general fund budget cuts."

Fiscal 2003 "(Appropriated) rainy day fund balance is estimated." Taken from NASBO (2002).

Table 2
The 12 Most Regressive General Sales Taxes in 2002
(Sales Tax Shares of Income by Family Income Group)

	Sales Taxes on Individuals		
State/Income Group	**Lowest 20%**	**Middle 20%**	**Top 20%**
1. Tennessee*	6.0%	4.1%	1.0%
2. Louisiana*	7.6%	5.4%	1.3%
3. Arkansas*	5.3%	3.5%	0.8%
4. Georgia*	4.5%	2.8%	0.7%
5. Florida	4.4%	3.0%	0.7%
6. Missouri*	4.7%	3.0%	0.7%
7. New Mexico*	7.3%	4.9%	1.4%
8. Mississippi*	**5.6%**	**3.9%**	**0.9%**
9. California	4.2%	2.7%	0.7%
10.Oklahoma*	4.6%	3.1%	0.8%
11. Alabama*	4.1%	2.6%	0.6%
12. Utah*	4.7%	3.5%	0.8%

* Sales taxes on groceries

Adapted from McIntyre, et al. (2003).

Section I

Background

Jean Honey (2002) presents a succinct analysis of the national economic picture and the related fiscal difficulties facing state governments. Honey explains fiscal 2000 as a peak year toward the end of an historic trend of a near-record economic expansion. At the end of that fiscal year, the states had a combined year-end balance equal to 10.4 percent of their budgets, representing one of the highest year-end balances in 20 years. In a fairly predictable response, 42 states subsequently lowered taxes by an estimated $5.2 billion.

> However, the euphoria of 2000 was followed by a sobering 2001. During fiscal year 2001, there was a precipitous decline in revenue growth. Revenues increased by a modest 4.5 percent — the slowest growth experienced since 1993 — in nominal terms (Honey, 2002).

This deflated revenue trend amounted to a real (adjusted for inflation) decline of more than 3 percent. One of the effects of the resulting recession was a significant budget shortfall in state goverments. In addition, there were other compounding problems impacting state fiscal outlooks. Unemployment rolls increased as a direct result of the recession. Also, a 14 percent increase in the costs of health care occurred, even before the attacks of September 11, 2001. Since then, 44 states have failed to reach projected levels of revenue, 19 states spent more than budgets allowed, and 36 states experienced budget shortfalls. The National Governors' Association projected the combined shortfall for all state governments in 2002 to total $25 billion (Honey, 2002). More recent reports indicate that the combined shortfall for state governments will reach $49.1 billion in fiscal 2003 and is likely to exceed $68.5 billion in fiscal 2004 (NCSL News, 2003).

The Fiscal Survey of States (National Association of State Budget Officers (NASBO), 2002) also provides insight into the national economic situation. According to the NASBO report, state revenues have dwindled across the nation as pressure on spending has increased. The largest budgetary items for state governments are, in order, elementary and secondary education (22.2 percent), Medicaid (19.6 percent), higher education (11.3 percent), transportation (8.9 percent), corrections (3.7 percent), public assistance (2.2 percent), and other expenditures (32.1 percent). A large part of state budgetary increases are directly attributable to increased spending on Medicaid, which grew 13.2 percent nationwide and over 25 percent in Mississippi in fiscal 2002, while other health care expenditures have grown over 14 percent. Because of a weak national economy, state tax collections have decreased to the point that combined general fund spending for all states in fiscal 2002 increased by only 1.3 percent over the previous fiscal year. Revenues for fiscal 2003 are expected to grow at about the same rate. This trend follows an 8.3 percent growth in fiscal 2001.

Surprisingly, in spite of the current crisis, the sentiment for tax cuts remains strong.

Some states have attempted to counter these trends by increasing taxes and fees, with the largest increases being implemented in taxes on cigarettes. This is often one of the easiest increases for lawmakers to justify, citing the increase as a means to protect public health. In fact, cigarette tax increases do little to reduce cigarette consumption and, indeed, the cigarette tax is considered a stable and safe source of additional revenue. It should be noted that lower-income people disproportionately represent cigarette smokers in Mississippi; therefore, this tax is extremely regressive.

Nationwide, general fund spending, as enacted in state budgets for fiscal 2003, grew by only 1.3 percent from previous levels, and 2002 levels were only 1.3 percent above fiscal 2001. These figures represent the smallest increase in state general fund spending since 1983 and demonstrate the inability to keep pace with inflation.

> Since the recession of the early 1990s, states have worked to build their rainy day fund balances and ending balances to safeguard against the disruption of services should economic growth slow. The fiscal downturn during those years and during a similar period in the early 1980s caused state balances to fall rapidly. During the one-year period from 1980 to 1981, for example, balances plunged from 9 percent of expenditures to 4.4 percent, forcing states to cut budgets and raise taxes. During the early 1990s, states found themselves lacking balances adequate to manage a fiscal slowdown once again. Before the economy slowed in 1989, state balances equaled 4.8 percent of expenditures. Within two years, balances hit bottom, totaling only 1.1 percent of expenditures in 1991. NASBO (2002) p. 13.

Given the recurrent pattern, it is apparent that budget difficulties following periods of expansion are quite likely. NASBO (2002) included a summary of Mississippi's general fund balance from 2001 through 2003 to demonstrate how the state's situation mirrored the rest of the United States. (See Table 1.)

NASBO (2002) also reported that after the budget passed in fiscal 2002, Mississippi's Department of Human Services received an additional budget cut. By Mississippi law a budget may be cut if, at the end of October, revenue falls more than 2 percent below estimates. This law provides flexibility for state budget expenditures, especially in situations where initial revenue estimates prove inaccurate.

During periods of economic prosperity, it is difficult to make political decisions regarding a possible economic downturn. Many state governments ignored the purpose of rainy day funds and the benefits of budget surpluses during prosperous economic times and chose instead to implement tax cuts. For example, consider remarks made by the treasurer of Mississippi:

> Certainly the time to consider tax relief is now, during flush economic times. Elected officials and those seeking elected office and citizens should educate themselves to tax relief which is most affordable, effective and does not jeopardize the provision of needed services and quality of life. Bennett (1999).

> Mississippi has weathered wilting revenue growth for three fiscal years and is positioned for a fourth straight year of under-performance in the economy. Revenue for fiscal year 2002, which ended June 30, actually fell below estimates by $268,000,000, and short of the previous year by $72.9 million (or -2.1 percent). While sales tax collections grew by almost 2 percent, individual income tax collections were 3.82 percent below the previous year, and corporate income tax collections posted a 7.10 percent decline. Budget safeguards enacted throughout the year, including reductions to estimates and budgets, tapping the rainy day fund, and transferring monies from the Health Care Trust Fund, allowed Mississippi to end the year with a balanced budget. . . . However, our budget safeguards were designed to offset two to four years of lagging revenue, and a buoyant economic recovery is not expected in 2003. We must be pragmatic in our approach and conservative in our budgeting and forecasting this year to avoid deep and painful budget cuts next spring. Bennett (2002).

Such reasoning is not unique. Much of the United States was also committed to tax cuts in 1999 and thought little about maintaining the integrity of rainy day funds. Surprisingly, in spite of the current crisis, the sentiment for tax cuts remains strong.

In addition, there is a small-government mindset among some politicians that cause them to seek tax cuts during tough times, eventually cutting services as a "necessary

Table 3
Shares of Family Income, Mississippi
(Non-Elderly) Paid for State and Local Taxes (2002)

Income Group	Lower 20%	Second 20%	Middle 20%	Fourth 20%	Top 20%		
					Next 15%	Next 4%	Top 1%
Income Range	**Less than $11,000**	**$11,000 to $19,000**	**$19,000 to $29,000**	**$29,000 to $53,000**	**$53,000 to $96,000**	**$96,000 to $228,000**	**$228,000 or more**
Average Income in Group	$7,000	$15,100	$24,100	$40,400	$69,000	$131,000	$509,000
Sales and Excise Taxes	**8.1%**	**8.0%**	**6.9%**	**5.4%**	**4.3%**	**2.7%**	**1.3%**
General Sales — Individuals	4.8%	5.0%	4.2%	3.5%	2.9%	1.8%	0.9%
Other Sales & Excise — Indiv.	1.2%	1.0%	0.9%	0.6%	0.4%	0.3%	0.1%
Excise Taxes on Business	2.1%	2.1%	1.8%	1.3%	1.0%	0.6%	0.4%
Property Taxes	**1.7%**	**2.9%**	**1.6%**	**1.4%**	**1.8%**	**1.8%**	**1.5%**
Property Taxes on Families	1.6%	2.7%	1.6%	1.2%	1.4%	1.2%	0.6%
Other Property Taxes	0.1%	0.1%	0.1%	0.2%	0.3%	0.6%	0.3%
Income Taxes	**0.2%**	**0.6%**	**1.2%**	**2.0%**	**2.4%**	**3.1%**	**4.0%**
Personal Income Taxes	0.1%	0.5%	1.2%	1.9%	2.4%	3.0%	3.8%
Corporate Income Taxes	0.1%	0.1%	0.0%	0.1%	0.1%	0.1%	0.2%
Total Taxes	**10.0%**	**11.6%**	**9.8%**	**8.8%**	**8.5%**	**7.6%**	**6.9%**
Federal Deduction Offset		0.0%	0.0%	-0.1%	-0.5%	-1.0%	-1.5%
Total After Offset	**10.0%**	**11.5%**	**9.7%**	**8.6%**	**8.0%**	**6.6%**	**5.3%**
Estimated % of taxes paid*	**15.5**	**5.12**	**6.82**	**18.0**	**32.6**	**9.7**	**10**
Estimated Cumulative % of taxes paid*	**15.5**	**20.6**	**27.4**	**45.4**	**78**	**90**	**100**

Adapted from McIntyre, et al. (2003).

* Estimated using Income Ranges and Burdens, McIntyre, and Family Income Distribution from SF3 Census 2000.

adjustment" to meet shortfalls.[1] For many lawmakers, economic downturns present an opportunity to downsize government.

Taxation Concepts

There are many types of taxes used for numerous purposes. State government revenue comes from a collection of sales, excise, and personal income taxes, while local government revenue relies primarily on the collection of property taxes. When the government implements taxes as a means to obtain necessary revenue, it may either be the change of an existing tax rate or the adoption of an additional tax. These concepts miss the important fact that taxes affect individuals, and these impacts create the distributional effects of taxation: the burden of taxation.

[1] *See, for example*, comments such as those of W. James Antle III (2001).

While there is great controversy about the degree that an individual should be taxed, some taxation principles are generally accepted. First, taxes should raise the greatest amount of revenue with the least amount of effort for all parties involved. Taxes should be *efficient* and *not interfere in the market process*, unless such interference is the reason for the tax. They should be *simple, easily administered*, and contribute to the *stability of revenue flows*, while providing *adequate revenue* for future uses. Also, it should be clearly apparent to the taxpayer that a payment is a tax, and the amount of the tax should be readily discernible to taxpayers. Finally, the tax should be *fair*.

These taxation principles present several contradictions. The first contradiction occurs between stability and fairness. The most progressive tax is a progressive income tax, while the most regressive tax is a sales tax. A sales tax, however, tends to be fairly stable during economic downturns, while a progres-

Table 4
Comparison of Mississippi to the 10 Most Regressive State Tax Systems.
Taxes as a Percent of Estimated income by
Shares of (Non-Elderly Taxpayers) Income (2000)

	Taxes as a Percent of Income on				
Income Group	Poorest 20%	Middle 60%	Top 1%	Poor/Top 1%	Middle/Top 1%
Washington	17.6%	11.2%	3.3%	537%	343%
Florida	14.4%	9.8%	3.0%	476%	325%
Tennessee	11.7%	8.9%	3.4%	347%	264%
South Dakota	10.0%	8.4%	2.3%	440%	369%
Texas	11.4%	8.4%	3.5%	331%	244%
Illinois	13.1%	10.5%	5.8%	224%	180%
Michigan	13.3%	11.2%	6.7%	199%	168%
Pennsylvania	11.4%	9.0%	4.8%	238%	187%
Nevada	8.3%	6.5%	2.0%	420%	331%
Alabama	10.6%	9.6%	4.9%	216%	195%
Mississippi	**10%**	**11.5%**	**6.9%**	**145%**	**167%**

Weighted averages based on McIntyre, et al. (2003), and estimated total income by group.

sive income tax tends to fluctuate with general economic activity (Fox and Campbell, 1984).

A second contradiction involves the very subjective concept of fairness, a concept often said to be "in the eye of the beholder." Fairness consists of two often contradictory principles: the "benefits principle" and the "ability-to-pay-principle." According to the benefits principle, taxpayers should pay a proportionate rate to the benefits derived from the use of their taxes. For example, those who drive should pay a gasoline tax to fund construction and maintenance of roads. This principle is often the reason for such taxation schemes as user fees, and these taxes typically ignore the taxpayer's level of income.

The second fairness concept is the "ability-to-pay-principle." According to this concept, those with greater resources should pay more in taxes. This concept is derived from a basic economic principle called the declining marginal utility of money. Simply stated, to individuals with great amounts of money, an additional dollar means very little; however, for individuals with very little money, an additional dollar is very important. Thus, a dollar of tax taken from a wealthy individual hurts less than the same amount taken from an individual with a lower income. The implication of this notion is that fair taxation would take proportionally more from wealthy individuals than from lower-income individuals.

Taxes have two basic economic effects. Taxes may alter the relative prices of goods and services, and because they tend to take more income from one group than from another, taxation tends to redistribute income. To examine tax incidence is to determine who bears the final burden of a specific tax or group of taxes. Taxes are classified according to incidence as regressive, progressive, or proportional with respect to an individual's income. A regressive tax is one in which the tax burden (defined as the share of income going to the tax) decreases as income increases. A tax is proportional when the tax burden is relatively constant across income groups. A tax is income-progressive when the tax burden increases as income increases. Under both progressive and proportional taxes, higher-income groups pay more than lower-income groups, but with a proportional tax, the percentage of income paid to taxes remains constant. With progressive taxes, the percentage of income increases as income increases.

Section II: Budget Revenues

The purpose of Section II is to examine the structure, incidence, and trends of Mississippi tax revenues during the period of 1998-2001, focusing specifically on three reasons lower-income families were affected by the existing tax structure.

> (1) The "new federalism" (or devolution) is becoming an increasing problem for states like Mississippi.
>
> (2) The need for additional tax revenues in Mississippi is increasing because of general economic conditions. Whether revenues are increased or services are decreased, there is likely to be a large difference in who bears the burden of these changes.
>
> (3) There is an increasing need to build both physical and social infrastructures for future economic growth.

"New federalism" refers to a general transfer of many of the traditional federal responsibilities to state and local governments, much of this without the commensurate shifting of revenue to those state and local authorities. New federalism revolves significantly around the changing welfare system. This includes how new welfare rules and the changed welfare system have affected low-income individuals. The changing ways in which income taxes affect the working poor are a partial focus of a multiyear study assessing new federalism by the Urban Institute (Maag and Rogers, 2002).

> Devolution is the term commonly used to describe the process by which the responsibilities of government are being shifted from federal to state and state to local governments. Much attention has been paid to the impact this shift may have on the services government

Table 5
Mississippi State Tax Commission General Fund Receipts

	1998 Total Collections	1999 Total Collections	2000 Total Collections	2001 Total Collections	2002 Total Collections
Sales Tax	$1,848,671,625	$1,980,897,637	$2,098,143,184	$2,111,495,133	$2,156,391,589
Individual Income Tax	$1,073,223,943	$1,209,892,383	$1,255,539,337	$1,293,424,736	$1,297,408,578
Corporate Tax	$314,574,060	$332,627,582	$325,114,162	$314,981,288	$296,158,407
Use Tax	$189,180,044	$213,363,728	$206,380,670	$204,687,299	$204,525,544
Gaming Fees and Taxes	$249,942,418	$279,277,415	$315,983,903	$320,509,123	$327,207,590
Insurance Premium Tax	$108,903,703	$109,016,942	$111,639,544	$117,114,909	$124,840,483
Tobacco Tax	$57,391,888	$56,981,138	$56,384,540	$55,507,295	$55,611,738
Alcoholic Beverage Tax	$44,680,886	$46,481,059	$48,177,235	$49,348,067	$50,912,397
Beer and Wine Tax	$28,764,878	$30,990,798	$30,801,274	$30,259,583	$30,627,521
Oil Severance Tax	$15,305,102	$8,041,735	$15,917,303	$27,629,713	$15,497,211
Gas Severance Tax	$10,038,762	$6,790,956	$8,782,543	$22,989,446	$12,703,748
Timber Severance Tax	$4,342,933	$4,242,671	$4,088,820	$3,751,441	$3,697,161
Estate Tax	$21,106,558	$30,766,896	$21,960,435	$27,574,705	$30,153,855
Auto Tag Fees	$105,610,471	$117,355,669	$124,900,497	$109,919,690	$96,053,695
Casual Auto Sales	$6,386,931	$6,644,033	$7,001,149	$6,758,864	$7,148,465
Installment Loan Tax	$7,490,469	$7,675,887	$8,043,793	$6,880,247	$10,306,979
Title Fees	$3,456,167	$3,926,833	$3,856,316	$3,677,988	$3,626,598
Petroleum Tax	$393,748,746	$400,071,243	$420,105,451	$407,054,380	$412,053,745
Miscellaneous Tax	$1,844,758	$2,878,004	$2,723,916	$423,959	$443,358
TVA in Lieu	$14,449,459	$15,239,689	$14,308,935	$14,595,138	$19,859,515
Nuclear in Lieu	$20,000,000	$20,000,000	$20,000,000	$20,000,000	$20,000,000
AMS Settlement				$25,000,000	$10,000,000
Other Collections	$45,943,469	$44,494,150	$49,251,517	$61,385,208	$60,768,432
Total Tax Commission Receipts	**$4,565,057,270**	**$4,927,656,448**	**$5,149,104,524**	**$5,234,968,212**	**$5,245,996,609**
Money Diverted	**$1,599,029,326**	**$1,736,150,564**	**$1,864,158,719**	**$1,897,472,231**	**$1,946,576,693**
Amount to the General Fund	**$2,966,027,944**	**$3,191,505,884**	**$3,284,945,805**	**$3,337,495,981**	**$3,299,419,917**

> provides. But, if state and local governments are to continue to provide the services they have in the past, and provide the new high quality services that the public demands, the discussion will inevitably turn to taxes (Ettlinger, O'Hare, McIntyre, King, Fray, and Miransky, 1996).

Robert Tannenwald, representing the Boston Federal Reserve Bank, has examined devolution by the federal government to the states. In his assessment, Tannenwald (1997) examined the "fiscal comfort" of each state as a function of state tax bases and state spending needs. Figure 1 represents his findings and indicates that Mississippi is the least fiscally comfortable state in the nation. (For figures, contact the authors.)

Ettlinger, et al. (1996) found that most state tax systems take proportionally more income from middle- and lower-income families than from wealthier families. In other words, most state and local tax systems are income-regressive. The Ettlinger study was updated in 2003 by McIntyre, et al., and published as "Who Pays" (2nd ed.). Both studies indicate that the characteristics that make a state tax system regressive include a reliance on sales and excise taxes rather than income tax and the use of a flat tax rate rather than a progressive income tax. It follows that states with less-regressive tax structures rely more heavily on a highly progressive income tax and less so on sales and excise taxes.

> On average, poor families pay more than six times as great a share of their income in state sales and excise taxes as do rich families, and middle-income families pay four times as great a share of their income in these consumption taxes as do the rich (Ettlinger, et al., 1996, p. 8).

There are two primary elements affecting the regressivity of any specific state tax system. First, it is important to decipher the differences in the effect that each tax has on taxpayers of different income levels. If the share of total income being paid in taxes is greater for lower-income taxpayers than for higher-income taxpayers, the tax is obviously regressive. The second important consideration when looking at an entire tax system is the extent to which each tax affects overall tax revenue. For example, while a state may have a highly progressive income tax, if the majority of tax revenue comes from sales tax (which is income-regressive), then the overall tax system is income-tax-regressive.

Types of Taxes

A general sales tax is among the most regressive types of tax. States that rely heavily on general sales taxes tend to have more regressive tax systems. Table 2 (see p. 850) is taken from Ettlinger, et al. (1996), and shows 12 states where the sales tax was most regressive in 1996. Mississippi is included as one of the 12 states.

Mississippi is the least fiscally comfortable state in the nation.

A sales tax is generally a fixed percentage of cost attached to a broad range of goods and (sometimes) services. The exact base for taxable sales varies substantially from state to state. Some states exempt food and/or drugs, and some allow additions to the base sales tax rate for local usage. Because sales taxes are imposed on the amount of expenditures, and because consumption generally decreases as a percentage of income as income grows, this tax is income-regressive.

An excise tax is usually confined to a relatively small group of goods and is levied on the quantity of goods rather than the expenditure on such goods. Wealthy taxpayers able to afford higher-priced goods actually pay the same amount of tax as lower-income taxpayers who may only be able to afford cheaper varieties. An excise tax constitutes a lower percentage of the price of a good as the price of that good increases. For example, the wealthier taxpayer tends to buy the most expensive items, therefore paying a lower percentage of tax on an item than a lower-income taxpayer. In this respect, an excise tax is even more regressive than a sales tax and is generally characterized as the single most regressive type of tax.

Most local government tax revenue is generated through property taxes on real and personal property of individuals and businesses. Property tax is generally regressive, but less so than sales and excise taxes. Real estate held by wealthy individuals tends to be a smaller share of their total income than real estate held by less-wealthy families. Generally, property is taxed at a flat percentage rate on a fixed proportion of the market value of the real estate. Many lower-income families rent and pay some portion of this tax in their rent payments, while middle-income families tend to concentrate wealth in the form of home ownership; consequently, property taxes hit middle-income households especially hard. Because lower-income families tend to pay a much higher share of total family income as rent than do wealthy families, the portion of the property tax passed on to renters also tends to be regressive. It has been argued by some proponents of consumption taxes that progressive taxes, such as the income tax, actually tend to reduce economic growth because higher-income individuals have less money to invest. From such reasoning, often called "Trickle-Down Theory," it is proposed that regressive taxes are better for economic growth than progressive taxes. However, research disputes this assertion. The degree of correspondence between the extent to which a state's taxes are regresssive and economic growth is not apparent.

> There is simply no correlation between the regressivity of a state's tax system and a state's income levels or income growth. Both the ten most regressive states and the ten least regressive have about the same average per capita personal income, and both had about the same average per capita personal income growth rates over the past seven years. Indeed, each of these groups was, on average, about the same in both categories as states in the middle of the pack (Ettlinger, et al. 1996).

The Institute on Taxation and Economic Policy has constructed a microsimulation tax model (Ettlinger, et al., (1996) and McIntyre, et al. (2003)). The major components of the model related to state income are state income tax, sales and excise tax, and property tax. The institute's estimation of tax incidence for these combined taxes for Mississippi is shown in Table 3 (see p. 852).

For the lowest 20 percent of income earners in Mississippi, 8.1 percent of family income for non-elderly families is paid in sales and excise taxes, 1.7 percent goes to property tax, and 0.2 percent goes to income tax, for a total of 10 percent of total family income allocated to taxes. For Mississippi families whose income is in the top 1 percent, income going to sales and excise taxes was 1.3 percent, property taxes was 1.5, and income taxes were 4 percent for a total of 6.9 percent. In general, the percentage of family income going to taxes decreases as income rises. This indicates that the system is indeed regressive. These figures clearly show that the share of income going to sales tax falls most dramatically with a regressive tax, and shares going to income tax increase, reflecting the progressivity of income tax. Also, it should be noted that in terms of regressivity the national average is relatively close to the average for Mississippi. Table 4 (see p. 853) compares the 10 most regressive tax systems with Mississippi's. While Mississippi is not one of the 10 most regressive states, it does have a highly regressive sales tax compared with other states. (See Table 2.) Thus, Mississippi's tax base is regressive, primarily because of a very regressive sales tax; the mildly progressive income tax does not significantly reduce this regressivity.

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Overall, Mississippi's state and local tax burdens are ranked relatively high by national standards (15th in 2002), even though the overall tax burden, including federal taxes, is ranked quite low (43rd in 2002) due to the progressive nature of the federal tax system (Tax Foundation, 2002). On the other hand, for per-capita taxes, Mississippi ranked 50th among all states due to Mississippi's overall low per capita income. Ettlinger, et al. (1996) reported that Mississippi is one of the 12 states with the most regressive state general sales taxes. The sales tax on individuals in the lowest 20 percent of family income groups

Table 6
Mississippi State Tax Commission General Fund Receipts
(In Real 1996 Dollars)

	1998 Total Collections	1999 Total Collections	2000 Total Collections	2001 Total Collections	2002 Total Collections
Sales Tax	1,771,776,524	1,844,239,491	1,873,676,714	1,835,923,079	1,843,069,734
Individual Income Tax	1,028,583,422	1,126,424,339	1,121,217,483	1,124,619,369	1,108,896,221
Corporate Tax	301,489,419	309,680,274	290,332,347	273,872,957	253,126,844
Use Tax	181,311,141	198,644,193	184,301,366	177,973,480	174,808,157
Gaming Fees and Taxes	239,546,117	260,010,628	282,178,874	278,679,353	279,664,607
Insurance Premium Tax	104,373,877	101,496,082	99,695,967	101,830,197	106,701,268
Tobacco Tax	55,004,685	53,050,124	50,352,331	48,263,017	47,531,400
Alcoholic Beverage Tax	42,822,394	43,274,424	43,023,071	42,907,632	43,514,869
Beer and Wine Tax	27,568,409	28,852,805	27,506,049	26,310,393	26,177,368
Oil Severance Tax	14,668,490	7,486,952	14,214,416	24,023,749	13,245,479
Gas Severance Tax	9,621,202	6,322,462	7,842,957	19,989,084	10,857,904
Timber Severance Tax	4,162,290	3,949,978	3,651,384	3,261,839	3,159,967
Estate Tax	20,228,635	28,644,350	19,611,033	23,975,919	25,772,526
Auto Tag Fees	101,217,626	109,259,537	111,538,218	95,574,028	82,097,175
Casual Auto Sales	6,121,268	6,185,675	6,252,142	5,876,762	6,109,799
Installment Loan Tax	7,178,905	7,146,343	7,183,241	5,982,303	8,809,384
Title Fees	3,312,408	3,655,929	3,443,754	3,197,972	3,099,656
Petroleum Tax	377,370,851	372,471,132	375,161,146	353,929,554	352,182,688
Miscellaneous Tax	1,768,026	2,679,456	2,432,502	368,628	378,938
TVA in Lieu	13,848,437	14,188,333	12,778,117	12,690,321	16,973,944
Nuclear in Lieu	19,168,104	18,620,240	17,860,332	17,389,792	17,094,017
AMS Settlement	0	0	0	21,737,240	8,547,009
Other Collections	44,032,460	41,424,588	43,982,423	53,373,801	51,938,831
Total Tax Commission Receipts	**4,375,174,689**	**4,587,707,335**	**4,598,235,867**	**4,551,750,467**	**4,483,757,785**
Monies Diverted	**1,532,518,043**	**1,616,377,026**	**1,664,724,700**	**1,649,832,389**	**1,663,740,763**
Amount to the General Fund	**2,842,656,646**	**2,971,330,308**	**2,933,511,167**	**2,901,918,078**	**2,820,017,023**

consumes about 5.6 percent of family income (in 1995) as compared with 6 percent in Tennessee, the most regressive sales tax state, and 4.7 percent in Utah, the 12th most regressive. This is largely due to assessing sales tax on groceries as well as general goods.

Mississippi's Tax Structure

An in-depth description of the Mississippi tax structure may be obtained from the Mississippi State Tax Commission, the source of the following information (Mississippi State Tax Commission, 2000). The commission lists the state's greatest sources of revenue as sales tax (41.1 percent), individual income tax (24.73 percent), petroleum tax (7.85 percent), gaming fees and taxes (6.24 percent), corporate income tax (5.65 percent), use tax (3.9 percent) and insurance premium tax (2.38 percent). (See Table 8, p. 859.) Mississippi's tax structure, like those of most states, is heavily dependent on sales, excise, and income tax, in addition to other smaller sources of revenue. Mississippi has a corporate as well as an individual income tax. The highest tax bracket is set at 5 percent for both. Appendix I contains a brief discussion and listing of Mississippi's specific tax categories. (Contact the authors for the Appendix.)

The income tax in Mississippi is mildly progressive and paid on the net taxable income of individuals, corporations, estates and trusts, and individual and fiduciary returns with the exception of qualified retirement income. The tax rate is 3 percent on the first $5,000 of taxable income, 4 percent on the second $5,000, and 5 percent on any remaining income. Exemptions vary for individuals from $1,500 (for the blind, those age 65 and over, or dependents), to $6,000 for individuals (whether filing separately or jointly), to $9,500 for heads of family. Deductions generally follow the same rules as federal law.

The single largest generator of tax revenue in Mississippi is the sales tax. The general retail sales tax rate is 7 percent, but there are lower rates for particular kinds of retail sales — including farm tractors, sales to electric power associations,

Table 7
Mississippi State Tax Commission Total Tax Receipts and Annual Percent Growth

	1998-1999 Percent Growth From Previous Yr.	1999-2000 Percent Growth From Previous Yr.	2000-2001 Percent Growth From Previous Yr.	2001-2002 Percent Growth From Previous Yr.	1998-2002 Average Annual Percent Growth
Sales Tax	4.09	1.60	-2.01	0.39	-0.97
Individual Income Tax	9.51	-0.46	0.30	-1.40	-1.81
Corporate Tax	2.72	-6.25	-5.67	-7.58	4.78
Use Tax	9.56	-7.22	-3.43	-1.78	0.93
Gaming Fees And Taxes	8.54	8.53	-1.24	0.35	-3.59
Insurance Premium Tax	-2.76	-1.77	2.14	4.78	-0.55
Tobacco Tax	-3.55	-5.09	-4.15	-1.52	3.93
Alcoholic Beverage Tax	1.06	-0.58	-0.27	1.42	-0.40
Beer and Wine Tax	4.66	-4.67	-4.35	-0.51	1.33
Oil Severance Tax	-48.96	89.86	69.01	-44.87	2.69
Gas Severance Tax	-34.29	24.05	154.87	-45.68	-2.85
Timber Severance Tax	-5.10	-7.56	-10.67	-3.12	7.93
Estate Tax	41.60	-31.54	22.26	7.49	-5.38
Auto Tag Fees	7.95	2.09	-14.31	-14.10	5.82
Casual Auto Sales	1.05	1.07	-6.00	3.97	0.05
Installment Loan Tax	-0.45	0.52	-16.72	47.26	-4.63
Title Fees	10.37	-5.80	-7.14	-3.07	1.72
Petroleum Tax	-1.30	0.72	-5.66	-0.49	1.79
Miscellaneous Tax	51.55	-9.22	-84.85	2.80	91.64
TVA in Lieu	2.45	-9.94	-0.69	33.76	-4.60
Nuclear in Lieu	-2.86	-4.08	-2.63	-1.70	3.03
AMS Settlement				-60.68	-25.00
Other Collections	-5.92	6.17	21.35	-2.69	-3.81
Total Tax Commission Receipts	**4.86**	**0.23**	**-1.01**	**-1.49**	**-0.61**
Money Diverted	**5.47**	**2.99**	**-0.89**	**0.84**	**-1.97**
Amount to the General Fund	**4.53**	**-1.27**	**-1.08**	**-2.82**	**0.20**

machinery sold to publicly owned port facilities, autos and light trucks, aircraft, farm implements, and materials for railroad construction. Also, a wholesale tax applies to alcoholic beverages, food and drink, and full-service vending machines. Plus, there is a sales tax on construction contracting, production involving natural resources, floating structures, public utilities, amusements, and several miscellaneous businesses. In addition, Mississippi has specific exemptions from sales tax, most of which involve agriculture, government, or production facilities. Finally, the state allows some special sales tax levies that vary by local jurisdiction from 1 to 3 percent.

After sales and income tax, one of the largest tax revenue sources in Mississippi is the tax on petroleum. The tax rate on automotive gasoline and undyed diesel fuel is 18 cents per gallon. Kerosene, fuel oil, and jet fuel are taxed at 5.25 cents per gallon, and a variety of other tax rates apply to compressed gas, liquefied compressed gas, and lubricating oils. Exceptions to the tax on petroleum are primarily made for the armed forces, the U.S. government, the state of Mississippi, and local governments.

Revenue Trends and Shares

Revenue for Mississippi by tax source is shown for 1998 through 2002 as nominal values in Table 5 (see p. 854) and in 1996 real dollars in Table 6[2] (see p. 856). Percent growth in revenue (in real dollars) is shown in Table 7, and each source of revenue as a percentage of total revenue is shown in Table 8. Table 8 also includes total tax revenue, the amount of that money diverted from the general fund, and the amount ending up in the general fund. Several important points should be noted. The largest single source of revenue (see Figure 1) is the general sales tax (40 to 41 percent of total revenue), followed

[2] Nominal values are deflated using the State and Local Government Implicit Price Deflator.

by individual income tax (23 to 25 percent); they demonstrate little growth in real terms after 1999.

Secondly, the percentage of total revenue diverted from the general fund consistently increased during the 1998-2002 period (see Figure 2, available from the authors, and Table 8), from 35 to 37 percent. Such revenue is diverted for a variety of reasons, including money paid to local governments and other special purposes. It is important to note that the increase in the percentage of money diverted from the general fund occurred simultaneously with the declining growth rate in all revenue. The result has been a general slowing of the growth rate in nominal revenue to the general fund: 7.6 percent from 1998 to 1999, 2.9 percent from 1999 to 2000, 1.6 percent from 2000 to 2001, and an actual decline from 2001 to 2002. In real dollars, adjusted for inflation, growth has been nearly stagnant, increasing only 0.23 percent from 1998 to 1999 and declining 1.01, 1.49, and 0.61 percent in the following three periods respectively. This decline occurred despite an infusion of AMS funds (from the accounting company lawsuit settlement) in 2001 and 2002 ($25 million and $10 million, respectively, in nominal values) and a sudden increase in "other collections" of about $10 million (nominal value) in 2001 that was sustained in 2002. Without consideration of these two sets of increased revenue, actual total revenue in nominal terms would have declined in both 2001 and 2002.

At this point, it should also be noted that the tax cut of Gov. Kirk Fordice (R) is of significant importance in these numbers. Like many other states, when revenue grew during the strong economic growth period of the 1990s, Mississippi decided to cut taxes significantly (Honey, 2002). Tax cuts included the elimination of capital gains taxes on gains in Mississippi and the elimination of the "marriage penalty." It is difficult to assess how these combined changes have affected current tax revenue. Similar tax cuts were made in many states around the same time because the surging economy gave a false sense of permanent prosperity and because cutting taxes received significant popular support. These tax cuts came as Congress began systematically devolving responsibilities to states without commensurate devolution of revenue. Circumstances have since changed. The long run of prosperity ended after fiscal 2000, which was the peak of fiscal surplus; this peak was followed by a sudden and significant reduction in state revenue in 2001. Nationwide revenue growth rates dropped to the lowest rates since 1993 (Honey, 2002), causing many states to experience budget shortfalls. The economic slowdown increased unemployment and caused a 14 percent rise in health care costs:

> Since this national disaster (the September 11 attacks), 44 states have faced lower than expected revenues, 19 have exceeded their budgets, and 36 have reported shortfalls. These budgetary crises were fueled partially by states' need to augment their security systems in the wake of September 11. According to a report issued by the National Association of Governors, the projected total shortfall for 2002 is $25 billion (Honey, 2002).

This revenue picture highlights the taxation principles of revenue stability versus revenue growth and fairness expressed as progressivity. During strong economic booms, revenue from a progressive income tax is likely to grow faster than a regressive sales tax. During economic downturns, income tax revenue tends to slow faster and in greater amounts than sales tax revenue. This causes many states to reserve sales tax money. In addition, the fairness concept of paying the same amount rather than paying according to the ability to pay remains important. For proponents of such sentiments, sales tax is the favored tax. Many individuals believe consumption taxes are more likely to reward saving. The degree to which such taxes discourage consumption and encourage savings is subject to significant debate.

Section III: State Expenditures

After adjusting for inflation, the Mississippi state budget increased by 21 percent from 1998 to 2002.[3] This represents an annual average increase of 5.2 percent in real appropriations. However, not all functions of Mississippi's government experienced real increases over this four-year period. Real appropriations for local assistance fell by 11 percent, while agriculture, commerce and economic development, and public health experienced a modest 4 percent decline. Section III analyzes trends in the state of Mississippi's budget by agency group and government function for the period of 1998 to 2002. In addition, this section addresses how changes in appropriations for particular budget categories might disproportionately affect lower-income individuals.

Trends in Appropriations by Agency Groups

The Mississippi budget has 102 categories when divided by agency groups. In these categories, real appropriations to 37 agency groups declined over the four-year period, and four groups were never funded. The most significant decline was for the Agribusiness Council, receiving real appropriations of $358,744 in 1998 but subsequently not funded in 2001 or 2002. The next most significant decline was in animal health, for which real appropriations fell by 43 percent. Social worker examiners, capital defense counsel, finance and administration, educational television, oil and gas, capital post-conviction counsel, public accountancy, and agriculture also saw real appropriations decline by 15 percent or more.

The most significant increase in real appropriations was for emergency management, which realized a gain of 303 percent between 1998 and 2002. Funding also increased by 91 percent for the Yellow Creek Inland Port Authority. Pat Harrison Waterway, soil and water, Grand Gulf Military Monument, Coast Coliseum, attorney general, secretary of state, Medicaid, Legislative Joint Operation, Treasury, marine resources, the Public Employees Retirement System, and public contractors also increased in real appropriations by 25 percent or more.

Trends in Appropriations by Government Function

When the budget is divided by function of government, 22 categories emerge. During the period studied, funding declined in three categories, and one category — transfers to reserves/writs/loans — was never funded. The most dramatic increase in real appropriations was for "non-budgeted 8000 funds" (bank accounts with special reporting requirements), which rose an incredible 21,029 percent. According to Deborah Collier Biggers, director of the Office of Budget and Fund Management (January 9, 2003), this was most likely because all 8000 funds were not reported in earlier

[3] This figure takes financial aid into account.

Table 8
Mississippi State Tax Commission General Fund Receipts as a Percent of Total Revenue

	1998	1999	2000	2001	2002
	Percent of Total	Percent of Total	Percent of Total	Percent of Total	Percent of Total
Sales Tax	40.50	40.20	40.75	40.33	41.11
Individual Income Tax	23.51	24.55	24.38	24.71	24.73
Corporate Tax	6.89	6.75	6.31	6.02	5.65
Use Tax	4.14	4.33	4.01	3.91	3.90
Gaming Fees and Taxes	5.48	5.67	6.14	6.12	6.24
Insurance Premium Tax	2.39	2.21	2.17	2.24	2.38
Tobacco Tax	1.26	1.16	1.10	1.06	1.06
Alcoholic Beverage Tax	0.98	0.94	0.94	0.94	0.97
Beer and Wine Tax	0.63	0.63	0.60	0.58	0.58
Oil Severance Tax	0.34	0.16	0.31	0.53	0.30
Gas Severance Tax	0.22	0.14	0.17	0.44	0.24
Timber Severance Tax	0.10	0.09	0.08	0.07	0.07
Estate Tax	0.46	0.62	0.43	0.53	0.57
Auto Tag Fees	2.31	2.38	2.43	2.10	1.83
Casual Auto Sales	0.14	0.13	0.14	0.13	0.14
Installment Loan Tax	0.16	0.16	0.16	0.13	0.20
Title Fees	0.08	0.08	0.07	0.07	0.07
Petroleum Tax	8.63	8.12	8.16	7.78	7.85
Miscellaneous Tax	0.04	0.06	0.05	0.01	0.01
TVA in Lieu	0.32	0.31	0.28	0.28	0.38
Nuclear in Lieu	0.44	0.41	0.39	0.38	0.38
AMS Settlement	0.00	0.00	0.00	0.48	0.19
Other Collections	1.01	0.90	0.96	1.17	1.16
Total Tax Commission Receipts	**100.00**	**100.00**	**100.00**	**100.00**	**100.00**
Money Diverted	**35.03**	**35.23**	**36.20**	**36.25**	**37.11**
Amount to the General Fund	**64.97**	**64.77**	**63.80**	**63.75**	**62.89**

years before the State Automated Accounting System (SAAS) was implemented. Non-budgeted 8000 funds serve mostly as clearing accounts for particular agencies. For example, child support payments are transferred from one parent to another through an 8000 account.

Real appropriations also increased significantly for fiscal affairs, rising at an annual rate of 38 percent. Debt service, executive and administrative, insurance and banking, miscellaneous, public protection and veterans' assistance, and social welfare also realized gains of 25 percent or more. The most significant decline was for local assistance, for which real appropriations fell by 11 percent.

Issues of Equity

One of the most common concerns of policymakers regarding equity revolves around tax burden and its influence on the distribution of income. However, changes in state spending can also influence population groups at different levels of income in disproportionate ways. Unfortunately, expenditure incidence is much more difficult to estimate than tax incidence. A basic equity problem is simply how to allocate the benefits from any public good or service. Tax payments are made in cash and are easy to measure, while public expenditure benefits are received in-kind and are much more difficult to track. Should a family's share of the benefits be in proportion to its income or to the number of family members (Menchik, 1991)? Furthermore, is the family the proper unit of analysis, or should policymakers be more concerned with how benefits accrue to an individual? These difficulties do not preclude a discussion of equity. However, the results presented in this section are merely suggestive.

Funding declined in real terms for several agency groups between 1998 and 2002. Funding declines most likely to affect Mississippi's low-income individuals include the following agency groups: community and junior colleges; social worker examiners; capital defense counsel; and capital post-conviction counsel. Although funding for community and junior colleges fell in real terms by only 4 percent, enrollment count and tuition costs have all increased. According to the U.S. Bureau of the Census, from 1998 to 2000, Mississippi's population of 18- to 24-year-olds increased by 3.7 percent (2001). According to the Mississippi State Board for Community and Junior Colleges (2001), the academic head count for the state's public community and junior colleges rose by 2.7 percent from fall 1999 to fall 2000. This increase in enrollment suggests that a decline in real appropriations for community and junior colleges will be severe if enrollment trends are not considered. When adjusting for inflation, rising tuition is also a concern in light of declined appropriations for community and junior colleges. According to the National Center for Public Policy and Higher Education (2002a), for families at the lowest end of income distribution in the nation, tuition at public two-year colleges and universities consumed 12 percent of family income in 2000. In 2002, the figure is even higher for Mississippians at the lowest end of income distribution; community and junior college expenses required 43 percent of family income (2002b). If Mississippi is to improve labor force skills and continue to provide access to postsecondary education for low-income students, an appropriation increase for community and junior colleges should be considered.

Real appropriations for social worker examiners declined by 39 percent from 1998 to 2002. This decline in appropriations may be a symptom of a much larger problem. As recently as June 2002, the Department of Human Services had 148 job vacancies in Mississippi. This large number of job vacancies may indicate that Mississippi does not have the necessary number of social workers required to meet its needs and ease the burden on existing employees (Sawyer, 2002). It is not surprising that the board responsible for licensing and regulating the state's social workers is unable to fill current vacancies due to lower appropriations of tax dollars. Any funding decline for this agency is alarming for three reasons: Mississippi is the state with the nation's highest percentage of low-birth-weight babies, and it is above the national average for both the percentage of births to teenage mothers (U.S. Census Bureau 2001) and the child poverty rate (Bennet and Lu, 2000).

Real appropriations for capital defense counsel and capital post-conviction counsel declined from 2001 to 2002 by 34 and 23 percent, respectively. In this short time frame, this decline is quite dramatic relative to other agency groups. The Mississippi Capital Defense Counsel was created by the Legislature in 2000 to provide counsel to indigent defendants possibly facing a death row conviction (Mississippi Code of 1972, as amended July 1, 2000). In 1999, 45 percent of individuals on death row in the nation were members of a minority group. Furthermore, the U.S. Bureau of the Census indicates that the majority of death row inmates have less than a high school (or an unknown) educational level. It is likely that cuts in appropriations to the capital defense counsel and the capital post-conviction counsel will disproportionately affect poverty-level individuals in Mississippi.

Appropriations for public health[4] also fell in real terms. The decline is minor (1 percent annually), and Mississippi ranks third in the nation in the percentage of total direct general expenditures by state and local governments devoted to health and hospitals. Such a large appropriation for public health spending is necessary because Mississippians spend little for personal health care and tend to be less healthy than residents of other states. Mississippi ranked 41st in personal health care expenditures.[5] Furthermore, the U.S. Bureau of the Census reports that Mississippi has more adult cigarette smokers than the national average based on the state population. Mississippi also leads the nation percentage-wise in the number of individuals defined as obese in 2000 (Centers for Disease Control). Regarding health insurance coverage, Mississippi lags behind the contiguous states of Alabama, Arkansas, and Tennessee. An alarming 16.6 percent of Mississippi's citizens did not have health insurance coverage in 1999 (United States Bureau of the Census). Furthermore, 15.5 percent of children in the state were not covered by health insurance in 1999; this figure is well above the national average of 13.9 percent. Such a lack of coverage indicates the vital role the state of Mississippi must play in providing public health for its citizens.

One of the greatest problems facing Mississippi (and many other states) in the current economic downturn is adequately funding Medicaid expenditures. Medicaid funding was the focus of a major controversy between Mississippi's governor and Legislature in 2002 (Smith, et al., 2002). At that time the Medicaid budget was expected to fall short $158 million in fiscal 2002 and $120 million in 2003 (Smith, et al., 2002). Gov. Ronnie Musgrove (D) signed a bill that included many cost-cutting provisions, including co-payment requirements and reduced reimbursement rates. Mississippi's governor and the Legislature had problems again agreeing on the 2003 bill. The governor vetoed the bill and warned that it would cause people to be thrown out of nursing homes and lose prescription drug benefits. The governor's veto was overridden, and the Mississippi Legislature instituted a quarterly budget cap. The fiscal 2003 budget for Medicaid was expected to face a shortfall in spite of a host of cost containment measures, including the following:

Provider Rates:

Most provider rates (excluding institutional providers) cut by 5 percent effective June '02.

In '02 and '03, provider taxes on nursing homes, intermediate care facilities for the mentally retarded (ICF/MRs) and psychiatric residential treatment facilities (PRTFs) increased with a new provider tax imposed on hospitals in '02.

Eliminated transportation reimbursement for attendant riders in '02.

Prescription Drug Controls and Limits:

In '02, reduced ingredient cost reimbursement from AWP-10 percent to AWP-12 percent in '02 and reduced dispensing fee from $4.91 to $3.91.

4 Public health includes all spending by the Mississippi Department of Health. The Medicaid Commission is included in social welfare.

5 Personal health care expenditures include, but are not limited to, hospital care, physician services, prescription drugs, and nursing home care.

Requiried the use of generic drugs when available and the return of unused drugs in tamper-resistant packaging originally dispensed for a nursing home patient.

Original plan to opt out of federal drug rebate program and establish a closed formulary that includes only drugs with the lowest and best price as determined through a bidding process was not approved by CMS. State now moving to adopt a preferred drug list.

In '02, reducing the maximum number of prescriptions per month from 10 to 7, with prior authorization required after 5.

In '02 limiting the quantity dispensed to a 34-day supply.

In '02 requiring that all Medicare-covered drug claims for dual eligible recipients be submitted first to Medicare before submission to the state.

Benefit/Service Reductions:

Reduced coverage for eyeglasses from one pair every three years to one pair every five.

Limited benefits for pregnant women to pregnancy-related services only in '02.

Shortened detoxification treatment days from 14 to 5-7.

Eligibility Reductions:

Eliminated declaration of income eligibility determination option in '02.

Other:

Maximum co-pays imposed on all possible services (ambulances, dental, federally qualified health center, rural health center, home health, hospital inpatient and outpatient, drugs, physician, eyeglasses, durable medical equipment), except for nonemergency transportation in '02.

Planning to implement disease management programs for asthma, diabetes, and hypertension in '03.

Eliminating the primary care case management program (Health MACS) in '02.

Looking at new fraud and abuses software and picture ID for recipients in'03.

Implementing emergency room diversions for non-emergency care in '02.

Departmental staffing freeze, travel restrictions and other administrative reductions in '02 and '03 (Smith, et al., 2002, p. 42).

There are two primary reasons for increased Medicaid costs: enrollment has increased and general health care costs have increased. In 1996, enrollment declined because the link between Medicaid and welfare eligibility was abolished. A large number of children, as many as 5 percent, were dropped from Medicaid eligibility (Smith, et al., 2002). After the 1997 State Children's Health Insurance Program (SCHIP) reduced eligibility requirements and improved administrative practices, enrollment of children surged. These changes, along with the increased unemployment rate, have contributed to the continued increase in Medicaid enrollment:

> The Urban Institute estimates that, starting from a base unemployment rate of 4.5 percent, every 1 percent increase in the unemployment rate adds about 1.6 million people to Medicaid enrollment. The unemployment rate as of August 2002 was 5.7 percent. Medicaid enrollment increased 3.5 percent in 1999 and increased 4.9 percent in 2000. Based on monthly enrollment data gathered through September 2001 from the states, the Kaiser Commission and HMA have estimated that in 2001 Medicaid enrollment increased 8.7 percent in 2001. In September 2001, total U.S. Medicaid enrollment reached 35.5 million (Smith, et al., 2002).

Medicaid costs have risen not only because of increased enrollment, but also because of the composition of the Medicaid population. About one-quarter of Medicaid enrollees are elderly or disabled individuals that require expensive medical services and pharmaceutical products.

> Using CBO estimates of this group (the elderly) accounts for approximately 67 percent of all Medicaid spending. Finally, the general rise in health care costs has increased the cost containment problem for state Medicaid budgets. KCMU has estimated that the majority (57 percent) of the $16 billion in federal Medicaid growth between 2001 and 2002 was due to spending on the elderly and disabled. Another 28 percent of the spending growth was attributable to spending on children and families and 15 percent was related to other factors, including states' use of upper payment limit arrangements (Smith, et al., 2002).

The Medicaid problem highlights one of the important philosophical disagreements in the era of devolution. Proponents of devolution maintain that states should be given the flexibility, along with the responsibility, for shouldering much of the costs for such programs. Opponents of devolving federal programs to the state level argue that such programs as Medicaid are really just government-provided insurance programs. Insurance only works well when large groups can spread both the risks and the financial responsibility. Pooling low-income, high-risk groups together and allowing high-income, low-risk groups to pool together separately (as is the de facto situation with Medicaid states) reduces the efficiency of cost sharing to benefit only lower-risk, wealthier areas.

Although individuals at or near the poverty level in Mississippi would likely benefit from increased funding for community and junior colleges, social workers, capital defense and post-conviction counsel, and public health, the state of Mississippi already appropriates a substantial amount of its budget to services that benefit the poverty-level population. For example, education accounted for 58 percent of general fund appropriations for the 2002 budget, and social welfare accounted for 10 percent (Joint Legislative Budget Committee, 2001). From 1998 to 2002, real appropriations for public education rose 18

Table 18
Shares of Family Income for
Non-Elderly Taxpayers State and Local Taxpayers, Mississippi (2002)

Income Group	Lowest 20 %	Second 20%	Middle 20%	Fourth 20%	Top 20%		
					Next 15%	Next 4%	Top 1%
Income Range	**Less than $11,000**	**$11,000 to $19,000**	**$19,000 to $29,000**	**$29,000 to $53,000**	**$53,000 to $96,000**	**$96,000 to $228,000**	**$228,000 or more**
Average Income in Group	$7,000	$15,000	$24,100	$40,400	$69,000	$131,000	$509,000
Sales and Excise Taxes	**8.1%**	**8.0%**	**6.9%**	**5.4%**	**4.3%**	**2.7%**	**1.3%**
General Sales — Individuals	4.8%	5.0%	4.2%	3.5%	2.9%	1.8%	0.9%
Other Sales & Excise — Indiv.	1.2%	1.0%	0.9%	0.6%	0.4%	0.3%	0.1%
Excise Taxes on Business	2.1%	2.1%	1.8%	1.3%	1.0%	0.6%	0.4%
Property Taxes	**1.7%**	**2.9%**	**1.6%**	**1.4%**	**1.8%**	**1.8%**	**1.5%**
Property Taxes on Families	1.6%	2.7%	1.6%	1.2%	1.4%	1.2%	0.6%
Other Property Taxes	0.1%	0.1%	0.1%	0.2%	0.3%	0.6%	0.3%
Income Taxes	**0.2%**	**0.6%**	**1.2%**	**2.0%**	**2.4%**	**3.1%**	**4.0%**
Personal Income Taxes	0.1%	0.5%	1.2%	1.9%	2.4%	3.0%	3.8%
Corporate Income Taxes	0.1%	0.1%	0.0%	0.1%	0.1%	0.1%	0.2%
Total Taxes	**10.0%**	**11.6%**	**9.8%**	**8.8%**	**8.5%**	**7.6%**	**6.9%**
Federal Deduction Offset		0.0%	0.0%	-0.1%	-0.5%	-1.0%	-1.5%
Total After Offset	**10.0%**	**11.5%**	**9.7%**	**8.6%**	**8.0%**	**6.6%**	**5.3%**

Source: McIntyre, et al., 2003.

percent, and social welfare appropriations rose 32 percent in real terms. In addition, Medicaid appropriations rose by 47 percent after adjusting for inflation.

Section IV: Conclusions and Recommendations

Conclusions

Taxes in Mississippi are regressive and inadequate to meet both the current and projected needs of the state. In 2001, Mississippi revenue and expenditures were $9.4 billion and $9.2 billion, respectively (Mississippi Department of Finance and Administration, 2002). Of these totals, $3.5 billion of the revenue came from the federal government. Some federal revenue is beyond the control of state government, but some is dependent on a match from the state; thus, the more the state can raise, the greater the amount that the federal government will give the state. Only $4.5 billion of revenue actually came from taxes, and only $3.3 billion is general fund revenue, or what many people regard as state revenue. In order to compare such figures across years, it is necessary to adjust these numbers to account for inflation, or what is referred to as "real" dollars. General fund revenue shown in Table 16 (contact the authors) is given in real 1996 dollars and has been adjusted for inflation using 1996 as the base year. Analysis of these numbers reveals that sales tax revenues, in real dollars, increased over the period 1998 to 2002, from $1.77 billion to $1.84 billion. Individual tax revenues over that same period rose from $1.03 billion to $1.11 billion. During the same period, corporate tax revenues dropped from $301 million to $253 million. Both in Mississippi and nationwide, state corporate tax revenue dropped during the incredible growth period experienced in the 1990s. No definitive explanation for this phenomenon can be found, so further investigation is warranted.

Finally, Table 16 shows that while total tax revenue remained essentially flat over the period studied, money diverted from the general fund increased, and the actual amount going into the general fund decreased, perhaps in part to a general trend of creating more special funds. Examples of such diversions include allocations of sales tax to local governments, gaming tax revenue to local governments, the educational enhancement fund, allocations to the Department of Mental Health, and funds for the Department of Transportation.

Table 17 (contact the authors) shows selected revenue sources as a percent of total Tax Commission revenues were calculated using data from the Comprehensive Annual Financial Report 2001 (Anderson, 2002). As shown in the table, both income tax and sales tax revenues declined as a percent of total tax receipts over the1998 to 2002 period, and corporate income tax declined as a percentage of total tax receipts from 6.89 percent in 1998 to 5.65 percent in 2002.

According to basic principles of taxation, taxes should be collected according to the principles of efficiency, the benefits principle, or the ability-to-pay principle, all of which suggest the implementation of progressive taxes. However, Mississippi taxes tend to be regressive, due to a significant reliance on a regressive general sales tax. It should also be noted that the recent trend of devolution of responsibilities from federal to state levels has not been followed with a concomitant devolution of funds. When funds are available from the federal government, they are often subject to a matching requirement from the state. This matching fund requirement is particularly difficult to meet when funds are needed most. It should also be recognized that individuals in very conservative political circles view this as part of a larger effort to cut both taxes and services in an effort to reduce the influence of government control. During fiscal difficulties, such as those currently experienced by Mississippi, this view suggests that it is better to cut services and taxes, rather than raise taxes to pay for services. Such views must be recognized by individuals seeking to deal with real tax revenue reductions.

Taxes in Mississippi are regressive and inadequate to meet both the current and projected needs of the state.

Tax incidence, or tax burden, refers to the percentage of an individual's income paid to taxes. In other words, the burden is the tax effort of specific groups of taxpayers. Taxes are regressive when taxes take an increasing share of income as income levels decline. Progressive taxes take an increasing portion of income for tax as income levels increase. It is sometimes stated that because wealthy individuals pay the majority of taxes, these individuals should also receive the majority of any tax cuts and pay a minority of any tax increases. Such views are contrary to the principle of the diminishing marginal utility of money, which suggests that individuals at high income levels get less satisfaction from an additional dollar of income than lower-income individuals, for whom similar increases in income are very meaningful. The validity of such a concept would suggest that progressive taxes are fairer than regressive taxes.

Table 18 shows shares of family income for non-elderly taxpayers in Mississippi in the year 2002 and allows the incidence of taxes in Mississippi to be examined. (For Tables 9-17, contact the authors.) Total taxes paid by those in the lowest-income bracket (less than $11,000) totaled 10 percent of family income, and rose for the second 20 percent (from $11,000 to $19,000) to 11.5 percent of family income. After that, as income rose the percentage of family income going to taxes steadily decreased. The top 1 percent of the income distribution ($228,000 or more) paid only 5.3 percent of its income in taxes. It is clear that Mississippi taxes are regressive primarily due to a highly regressive sales tax. It is also clear that the state's income tax is only mildly progressive. In addition, property taxes imposed at local levels of government would be much more regressive if Mississippi did not allow an exception for homestead exemptions.

A comparison of tax incidence for neighboring states (Louisiana, Tennessee, Arkansas, and Alabama) and for comparison states (Arizona, Maine, North Carolina, and North Dakota) is shown in Table 19 (next page). States used for comparison to Mississippi were chosen based on similarities in population densities and industrial bases.

Table 19 shows that while Mississippi is regressive in taxation, it is by no means the most regressive of the neighboring and comparison states. Tennessee is far more regressive than Mississippi, largely because the state relies predominantly on sales tax for revenue. Such states as Maine, where food is exempt from sales tax and income tax is highly progressive, is considered to be far less regressive.

Although tax revenue has slowed and even declined for some sources of revenue in Mississippi, expenditures have continued to increase. Figures 4 and 5 (contact the authors) show examples of these trends in real 1996 dollars. Education, public welfare, health, highways, corrections, and natural resources are all particularly noteworthy for their rapid increases in expenditures. Slowing revenue and increasing need for revenue leaves the state with two options: revenue must be increased, or expenditures must be reduced. Many areas of expenditures, such as those by the Department of Human Services, have seen such drastic budget cuts that they are unable to fully participate in federal programs when matching funds are required for eligibility. Part of the existing revenue problem is due to the slowing economy, as well as the concerns of many voters and politicians about the proper role of government and taxation. Some individuals want decreased taxes rather than increased expenditures but have not clearly indicated how services would be provided in the absence of these expenditures. In the areas of health care and Medicaid, expenditures will likely continue to grow. This leads to the conclusion that some form of tax increase, rather than tax relief, is needed. Given the current tax burden, the need for substantial revenue, and the history of revenue contributions, Mississippi's three obvious sources for increased revenue include:

- personal income tax;
- corporate income tax; and
- tax exemptions.

Recommendations

Mississippi's personal income tax is among the flattest state income taxes in the nation. One possible remedy to increase tax revenue is to make the income tax more progressive. This could be accomplished by raising the tax rate for the top income bracket or by adding additional income brackets with higher tax rates. For example, adding a fourth income bracket, $5,000 higher than the existing highest bracket, and giving that tax bracket a 1 percentage point higher tax rate could increase tax revenue by a minimal estimate of $248 million.

One possible remedy to increase tax revenue is to make the income tax more progressive.

An increased corporate income tax is another possible source of additional revenue for the state. Mississippi is already a pioneer in solving the passive investment corporate loophole (Mazerov, 2002). Mississippi should also remedy other possible tax loopholes that may exist. The Tax Commission must respond to the drop in revenue received from state corporate income tax during a time when federal corporate income tax has increased. If revenue from corporate tax supplied the same portion of total revenue going to the Tax Commission as in 1998 (6.89 percent compared with 5.65 percent now), corporations would have paid an additional $65,290,759 in corporate income tax.

Finally, many tax exemptions exist in the state tax structure. Some tax exemptions should certainly be kept, an example being personal exemptions from individual income tax. However, all exemptions and the cost of those exemptions should be examined. The report to the State of Mississippi Tax Commission titled *The Annual Tax Expenditure Report*, produced

Table 19
Shares of Family Income for Non-Elderly Taxpayers
State and Local Taxpayers (2002)

Income Group	Lowest 20 %	Second 20%	Middle 20%	Fourth 20%	Top 20%		
					Next 15%	Next 4%	Top 1%
Income Range	**Less than $11,000**	**$11,000 to $19,000**	**$19,000 to $29,000**	**$29,000 to $53,000**	**$53,000 to $96,000**	**$96,000 to $228,000**	**$228,000 or more**
Average Income in Group	$7,000	$15,100	$24,100	$40,400	$69,000	$131,000	$509,000
State							
Mississippi	10.0	11.6	9.8	8.8	8.5	7.6	6.9
Neighboring States							
Louisiana	11.5	10.6	9.5	8.7	7.5	6.6	6.0
Tennessee	11.7	10.5	8.8	7.4	6.2	4.5	3.4
Arkansas	10.7	10.9	10.5	9.6	9.4	8.8	7.8
Alabama	10.6	10.5	10.9	8.4	7.3	6.1	4.9
Comparison States							
Arizona	12.5	10.8	9.7	8.9	7.9	7.0	6.6
Maine	10.0	10.3	10.2	10.5	10.9	10.5	9.7
North Carolina	10.7	10.1	10.2	9.9	9.7	9.1	8.9
North Dakota	10.2	9.5	9.1	8	7.7	6.4	6.5
Source: McIntyre et al., 2003.							

by the Center for Policy Research and Planning at the Mississippi Institution of Higher Learning, provides valuable information for this purpose. The Legislature should review this document annually and determine which exemptions remain appropriate and which may be eliminated. Also, estimates of tax expenditures for the Mississippi Advantage Jobs Incentive Program and the Growth and Prosperity Area should be made. Records of both are shown as "not available" for fiscal 2003.

A key question in the overall tax debate concerns economic development. Some developers suggest it is necessary to provide large tax breaks and low tax burdens to business in order to improve economic development. A large body of economic literature exists to refute this assertion and suggests that a state's business structure has little, if any, impact on economic development. An example is the work by Robert Tannenwald of the Boston Federal Reserve Bank (Mazerov, 2002, addresses this work). Tannenwald found no statistical correlation between business tax burdens and the location of new investments.

Increasingly, economists specializing in economic development are finding that the most important factor influencing the location of firms, especially in the case of firms with high-quality, high-wage jobs, is the quality of life in a community. Improving the quality of life requires adequate education, social services, health care, and infrastructure development. In places where this has been the primary goal, not only has development not been impeded, but firms have also often been willing to pay impact fees to offset the costs of supporting local economic development. Ultimately, improving quality of life will require substantial expenditures; this will likely cause state policymakers to consider how best to increase state revenues.

Mississippi's Tax Structure

Mississippi collects taxes through at least 25 specific tax and fees categories:

(1) Ad Valorem
(2) Alcoholic Beverage
(3) Beer and Light Wine
(4) Certificate of Title for Motor Vehicle
(5) City Utility
(6) Corporate Organization and Qualification
(7) Corporate Franchise
(8) Estate
(9) Gaming License
(10) Hazardous and Nonhazardous Waste
(11) Income
(12) Insurance
(13) Insurance Premium Tax
(14) Motor Vehicle Rental Tax
(15) Petroleum
(16) Privilege, Local
(17) Privilege, Statewide
(18) Public Utilities
(19) Sales
(20) Sales-Special Tax Levies
(21) Severance
(22) Tire Disposal Fee
(23) Tobacco
(24) Unemployment Insurance
(25) Use 911 Emergency Telecommunications Training Fee

The ad valorem tax is a property tax on real and personal property. The property is appraised for true value and then taxed at a percentage of the value. Local governments collect this tax, except in the case of public services, such as power and light, telephone, and railroad. There is a homestead exemption from certain ad valorem taxes, which varies according to the assessed value of the house and whether the owner is age 65 or over or disabled. Exemptions also exist for free-port warehouses and certain industries, except for that portion of the ad valorem tax used for school district purposes.

Taxes on alcoholic beverages include permits for manufacturing, retailing and excise tax on distilled spirits ($2.50 per gallon), sparkling wine and champagne ($1.00 per gallon), and wine (35 cents per gallon). In addition, a markup of 27.5 percent is mandated and includes a 3 percent markup designated for the Division of Alcohol and Drug Abuse of the State Department of Mental Health. Beer and light wines are taxed separately from alcoholic beverages and include licenses, permits, and excise tax. Excise tax is 42.68 cents per gallon and paid by wholesalers, and collected by the Miscellaneous Tax Bureau of the Tax Commission.

Fairly minor taxes and fees accrue from certificates of title for motor vehicles and fees for corporate organizations and qualifications. City utility tax is collected from telephone and communication utilities, but the amounts are passed to the municipality, less a 5 percent administrative fee. Estate tax with a statutory exemption of $600,000 for all decedents dying on or after October 1, 1990, is also in place. Otherwise, the tax rate varies from 1 to 6 percent, depending on the size of the estate. Gaming license fees include fees on establishments, on the number of games, gross revenue as well as municipal and county fees passed along to those entities by the Miscellaneous Tax Bureau of the Tax Commission.

Hazardous waste and nonhazardous solid waste tax is collected from commercial waste management facilities at the rate of $10 per ton for hazardous waste generated and disposed by land filling. Hazardous waste generated and treated in the state, or stored for less than one year is taxed at a rate of $2 per ton, while hazardous waste generated and recovered in the state is taxed at a rate of $1 per ton. Hazardous waste imported into Mississippi is charged a fee equal to the per-ton fee imposed by the state of origin. Commercial nonhazardous waste is charged a tax fee of $1 per ton.

Tax on capital gains follow the federal tax code. Sales tax is 7 percent throughout the state with optional additions to this rate by specific local jurisdictions. Automobile tax includes a flat-rate tax charge and an ad valorem tax for the city and the county. The rate varies according to the age and value of the car. Real estate tax on residences is assessed at 10 percent of their real value and then a millage rate is imposed on that assessed value. The millage rate generally falls between 75 and 100 percent in Mississippi. In addition to the major taxes listed that directly affect most individuals, Mississippi also taxes petroleum and casinos. There are specific exemptions for the elderly, including exemptions on sales tax for prescription drugs, homestead exemptions and age credits on homes, and exemptions from income tax on retirement funds. In addition, Mississippi exempts many businesses from ad valorem tax and sales tax at a rate lower than the general sales tax rate.

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