Policy Matters Ohio

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Taxes & Ohio Budget

Ohio needs a corporate profits tax

Beneficiaries of the pandemic should pay up

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Corporations can't operate without using our collective public resources. They need a well-trained, educated and healthy workforce. Public roads and airports are necessary to move their products to market. Yet Ohio is one of just six states with no state-level corporate income tax. This means that corporations that are profiting immensely from the pandemic are not contributing commensurately to providing public services funded by the state. That needs to change.

Millions of Ohioans are hurting – claiming unemployment benefits, needing food assistance, fearing that they could lose their homes. Even while many people are having a hard time meeting their basic needs, our lawmakers are not making sufficient investments vital to our long-term success, like public education, high quality child care and broadband infrastructure. In the face of a pandemic and recession, a status quo state budget that just preserves existing initiatives is not enough.

A corporate profits tax would help lawmakers avert budget cuts and make the long-term investments we so badly need. Reinstating that tax, which lawmakers repealed in 2005, also would make Ohio's tax system more fair, since it is one of the few taxes based on ability to pay. Though it had many caveats and was at most a rough estimate, an analysis prepared by the Legislative Service Commission at the request of state Rep. Michael Skindell found that such an 8.5% tax could provide nearly $500 million a year in revenue. The Institute on Taxation and Economic Policy, a national nonprofit with a model of the tax system, confirmed such a broad-based tax could bring significant revenue.

Pandemic profits

While many small businesses struggle to stay open, more than a few big companies are reaping benefits from the pandemic. From toymakers to delivery services, online retailers to makers of cleaning products, some are cleaning up. Profits at Amazon.com Inc., for instance, nearly tripled in the third quarter, to $6.3 billion. At FedEx, profits nearly doubled in the quarter ended Nov. 30.

Overall, Ohio business has profited from significant tax cuts, and business taxes in Ohio are lower than in other states. The tax overhaul that eliminated our corporate income tax in 2005 as well as a major property tax on business and substituted the Commercial Activity Tax

(CAT), a tax on Ohio gross receipts, is costing $1 billion or more a year. A report by Ernst & Young details how Ohio's combined state and local taxes on business are considerably lower than the national average as a share of private-sector output and per employee. Yet Ohio incomes have continued to trail the national average, while job growth even before the pandemic was weak.

One way to reinstate a corporate income tax in Ohio is to follow the basic idea behind the old corporate franchise tax. Nonfinancial companies figured out how much they would pay under two different methods, one based on net income, the other on their net worth, and paid whichever was higher. Similarly, companies now could continue paying the CAT or, if their computed corporate income tax was higher, pay that instead. The smallest companies would be exempt or pay a flat $150, as with the CAT. Only profitable companies would wind up paying more.

One of the weaknesses of the old corporate franchise tax was that it excluded S Corporations, limited liability companies (LLCs) and others known as "passthrough entities" because their profits are taxed under the individual income tax as they pass through to their owners. Ohio already provides a giant tax break to owners of such entities, exempting the first $250,000 in such income and taxing such income over that amount at a special, low rate. This costs more than $1.17 billion a year, without showing real results in additional small business hiring. A reinstated Ohio corporate income tax should cover large passthrough entities, which should not get special treatment.

Lawmakers should also pass a corporate profits tax that limits tax avoidance, a major defect in the old Ohio tax. They can treat corporations composed of a parent and its subsidiaries as a single entity for tax purposes. Twenty-seven of the 44 states with a corporate income tax have adopted this practice, known as combined reporting. Ohio should adopt a strong form of it.

Only profitable companies pay a corporate profits tax. Most young, expanding companies are unlikely to be affected by the addition of such a tax.

Moreover, a corporate profits test would be a step toward reforming our upside-down state and local tax system, under which the poorest Ohioans on average pay almost twice as much of their income as the top 1% making more than $490,000 a year. A corporate profits tax is just one part of reforms that are necessary to provide the revenue for the public services that would allow all Ohioans maximum opportunity, regardless of where they live and whether they are Black, white or brown. Ohio needs to reinstate a tax on corporate profits.