Policy Matters Ohio

POLICY BRIEF

June 2024

Income tax extremism is a gift to the wealthy. Repairing the damage would cost us all.

Bailey Williams

Ohioans deserve an equitable tax system that supports the public goods and services that enable all of us to thrive. Unfortunately, that is not the system we have today. After two decades of tax handouts to corporations and the rich, our upside-down tax system increasingly perpetuates inequality while failing to adequately fund services like education and health care.[1] This all pales in comparison to the extreme proposal from lawmakers that would eliminate the state's personal income tax.[2]

Income tax elimination effects

The Institute on Taxation and Economic Policy (ITEP), a Washington, D.C., nonprofit with a sophisticated model of the state and local tax system, modeled what an income tax repeal would look like in Ohio. The biggest beneficiary of this repeal would be the wealthiest Ohioans. An income tax repeal would see the state losing just over $11 billion in revenue, with the top 20% of earners, meaning those with incomes above $133,900, capturing 69.64% of the tax cut's value. By comparison, the bottom 60% of Ohio earners, or those making less than $79,200, would see just 11.21% of the value of tax cut.

[See Table 1 on the following page.]

[1] Bailey Williams, Ohio's tax system perpetuates inequality. Policy Matters Ohio. January 9, 2024.

[2] Two companion bills have been introduced in the 135th General Assembly to eliminate both the Personal Income Tax: S.B. 216 and H.B. 386. Each bill will phase out both the Personal Income Tax and the Commercial Activity Tax (CAT), but they do so at different rates per year. Policy Matters Ohio will cover the CAT repeal in the near future.

Policy Matters Ohio

Table 1

Income tax repeal: A gift to the wealthiest

Tax changes resulting from a repeal of Ohio's personal income tax, by income distribution, in 2024 income.

2024 Income	Lowest 20%	Second 20%	Third 20%	Fourth 20%	Next 15%*	Next 4%*	Top 1%*
Income Range Start	**Below**	**$25,500**	**$49,000**	**$79,200**	**$133,900**	**$252,400**	**$677,000**
Income Range End	**$25,500**	**$49,000**	**$79,200**	**$133,900**	**$252,400**	**$677,000**	**And Above**
Average Income	**$14,400**	**$37,000**	**$63,700**	**$102,700**	**$170,800**	**$371,500**	**$1,580,500**
Average Tax Change	-$1	-$257	-$733	-$1,691	-$3,600	-$7,503	-$38,737
Share of Resident Tax Cut	0.01%	2.90%	8.29%	19.16%	30.47%	17.17%	22.00%
% with Tax Cut	0.26%	45.28%	76.25%	94.67%	97.65%	96.16%	100.00%
Avg. Tax Cut for Those with Cut	$487	$567	$962	$1,786	$3,687	$7,802	$38,737

ITEP's model uses a definition of income that differs slightly compared to Ohio Adjusted Gross Income. The model includes some taxable income streams and some income streams that are not taxable under Ohio AGI. This is why some residents in the lowest income distribution appear to receive to a tax cut, even though Ohioans making less than $26,050 a year do not pay the state personal income tax.
**Combined, the columns to the right of the red line represent the wealthiest 20%.*

The personal income tax enables the state to provide a plethora of robust public services that improve the quality of life for Ohioans. In Fiscal Year 2023, the state personal income tax brought in over $10.7 billion in revenue to the General Revenue Fund (GRF), which equates to 37% of all state revenue deposited into the GRF. 3.4% of all income tax revenue is dedicated to supporting local governments and public libraries. The income tax also allows the state to provide property tax relief without harming the local entities that rely on that revenue.

Eliminating the income tax would devastate the quality of services the state provides for millions of Ohioans. Ohio spent just over $40 billion from the GRF in fiscal year 2023.[3] Assuming no further tax changes to make up the revenue loss, the state would have to cut

[3] Ross Miller, LBO Budget Footnotes. Legislative Service Commission. July 2023.

almost a quarter of its spending to balance the budget from a $11 billion deficit.[4] That would be the same as completely cutting state funding for public K-12 education.[5]

This income tax repeal would also make Ohio's tax system overly reliant on regressive forms of taxation. Over the last two decades, Ohio has become increasingly dependent on the sales tax to make up for revenue lost from a generation of income tax cuts. Since 2014, the sales tax has been the largest source of state tax revenue. For context, the income tax was the largest source of revenue for every year in between 1984 and 2014, except for one.[6] In fiscal year 2023, the sales tax accounted for 46.6% of GRF revenue, while the income tax's share equaled 37.3%. Should the income tax be eliminated, an overwhelming majority of Ohio's tax revenue will come from the regressive sales tax with drastic budget cuts needed to balance our budget as required by the state constitution. Additional revenue would be needed to make up billions of dollars no longer available. Further ITEP modeling provides a look into what this tax system might look like.

Replacing 50% of personal income tax revenue with increased sales tax

ITEP has provided modeling on a hypothetical sales tax rate increase should the state repeal the personal income tax. To make up just 50% of the $11.1 billion in lost income tax revenue, which would still leave a yawning budget hole, the state sales tax rate would have to increase from 5.75% to at least 8.07%. This 8.07% sales tax would be the highest in the country, surpassing California's 7.25% state sales tax.[7]

When considering local county and transit taxes, Ohio's average combined state and local sales tax rate would jump from 7.24%, the 21st highest in the country, to 9.56%, tied with Louisiana for the highest combined rate in the U.S.[8] Combined state and local sales tax rates in Ohio would range from as low as 8.82% in four counties to a high of 10.32% in Cuyahoga County.[9] Four Ohio counties, Cuyahoga, Hamilton, Lucas, and Coshocton, representing over 20% of Ohio's population, would each have a combined state and local sales tax above 10%.[10]

The modeling done by ITEP also provides a breakdown of how an income tax repeal coupled with a sales tax increase to 8.07% would impact Ohioans by income distribution. The results from this sales tax increase are highlighted in Table 2 below. As with earlier tax

---

4 NOTE: The personal income tax receipts cited provides for just the share of the personal income that is deposited into the General Revenue Fund. This does not include the 3.4% of total personal income tax revenue that is split evenly between the Local Government Fund and the Public Library Fund. When adding the 3.4% into total personal income tax receipts, the revenue comes out to over $11.1 billion for Fiscal Year 2023. Kimberly Murnieks, OBM Director, State of Ohio Monthly Financial Report. July 10, 2023. See Table 1 General Revenue Fund Receipts. Actual FY 2023 Personal Income Receipts.

5 In the most recent state operating budget bill, H.B. 33, $11.2 billion and $11.5 billion were appropriated for K-12 Education for fiscal years 2024 and 2025, respectively.

6 Selected Ohio Tax Sources Administered by the Tax Commissioner. Ohio Department of Taxation. February 12, 2024.

7 Jared Walczak, State and Local Sales Tax Rates, 2024. Tax Foundation. February 6, 2024. See "State and Local Sales Tax Rates, 2024" Table.

8 In the above source, see "Combined Rate" column.

9 Rates found by adding the difference (2.32%) between the hypothetical new sales tax (8.07%) and the current Ohio sales tax (5.75%) to current combined state and local sales taxes for each Ohio counties. Local sales taxes include sales taxes levied by counties and by transit authorities. Four counties with lowest combined state and local sales are Butler, Stark, Lorain, and Wayne (current rate: 7.25%.) The four counties with highest combined rates are Cuyahoga (8%), Hamilton (7.8%), Lucas (7.5%), and Coshocton (7.5%.)

10 These four counties account for 21.72% of Ohio's Population according to the 2020 U.S. Census. U.S. Census Bureau. (2020). RACE. *Decennial Census, DEC Redistricting Data (PL 94-171), Table P1*. Retrieved May 23, 2024.

policy, it is the wealthiest Ohioans who benefit at the expense of those with low or moderate incomes.

Table 2

Raising OH sales tax to the nation's highest would only cover half the lost revenue.

Tax changes resulting from a repeal of Ohio's personal income tax + sales-tax increase to 8.07%, by income distribution, in 2024 income.

2024 Income	Lowest 20%	Second 20%	Third 20%	Fourth 20%	Next 15%	Next 4%	Top 1%
Income Range Start	Below	$25,500	$49,000	$79,200	$133,900	$252,400	$677,000
Income Range End	$25,500	$49,000	$79,200	$133,900	$252,400	$677,000	And Above
Average Income	$14,400	$37,000	$63,700	$102,700	$170,800	$371,500	$1,580,500
Tax Change as % of Income	1.21%	0.41%	-0.21%	-0.81%	-1.43%	-1.58%	-2.24%
Avg. Total Change (Income Tax Cut + Sales Tax Increase)	$174	$153	-$131	-$827	-$2,435	-$5,874	-$35,366
Avg. Change from Sale Tax Increase	$175	$409	$603	$864	$1,165	$1,628	$3,370

ITEP's model uses a definition of income that differs slightly compared to Ohio Adjusted Gross Income. The model includes some taxable income streams and some income streams that are not taxable under Ohio AGI. This is why some residents in the lowest income distribution appear to receive to a tax cut, even though Ohioans making less than $26,050 a year do not pay the state personal income tax.
**Combined, the columns to the right of the red line represent the wealthiest 20%.*

Ohioans among the top 1% of earners, with incomes above $677,000, would see an average tax cut of $35,366. Meanwhile, the average Ohioan in the bottom 40% of earners would see a net tax increase from this policy change. The lowest 20% of earners with incomes below $25,500, would see an average tax increase of $174. The second quintile of earners, with incomes between $25,500 and $49,000, would see a $153 tax increase on average. It is simply unconscionable to give a $35,000 tax cut to the wealthy by forcing those who struggle to make that amount in a year to pay for it.

After decades of gradually eroding the personal income tax, lawmakers have proposed eliminating the income tax by 2030. Let’s be clear, this is a truly radical proposal. No state has eliminated their personal income tax since 1980, when Alaska experienced their major oil boom.[11] For the nine states without a personal income tax, the claim they are "low tax" states only applies to the rich. Across these states, the bottom 20% of earners pay an average of 11.6% of their income in state and local taxes, ranging from a low of 8.7% in Alaska to a high of 13.8% in Washington state. Meanwhile, the top 1% pay on average 3.3% of their income in these taxes, from a low of 2.6% in South Dakota and a high of 4.6% in Texas. To illustrate this point, take Florida, Tennessee and Texas, three states without a personal income tax, compared to three states often branded as "high tax" states: California, Massachusetts and New Jersey. Table 3 below compares the share of income dedicated to paying state and local taxes in these states, plus Ohio.[12] Earners in the lowest two quintiles pay a greater share of their income in these taxes in all three states without an income tax. Meanwhile, the top 1% pays anywhere from roughly 65% to 80% less in state and local taxes compared to the poorest earners.

Table 3

"Low tax" states? Only for the wealthy.

Total state and local taxes as a share of family income by income distribution.

State	Lowest 20%	Second 20%	Middle 20%	Fourth 20%	Next 15%*	Next 4%*	Top 1%*
Ohio	12.7%	10.5%	10.4%	10.0%	9.3%	8.0%	6.3%
Florida	13.2%	10.9%	9.5%	8.4%	6.4%	5.0%	2.7%
Tennessee	12.8%	10.9%	10.2%	8.6%	7.1%	5.3%	3.8%
Texas	12.8%	11.2%	9.9%	8.8%	7.2%	6.2%	4.6%
California	11.7%	10.3%	10.4%	11.0%	10.8%	10.4%	12.0%
Massachusetts	8.2%	9.2%	9.6%	10.0%	9.1%	7.9%	8.9%
New Jersey	8.8%	9.4%	10.8%	12.0%	11.1%	9.4%	10.5%

**Combined, the columns to the right of the red line represent the wealthiest 20%.*

The main driver for this discrepancy in taxes paid can be attributed to the forms of taxation relied on in these states. Among the three main forms of taxation in the U.S. — property, sales, and income — the income tax is the only one that considers one's ability to pay. Most states, including Ohio, use a progressive income tax with graduated brackets that increase with one's income.[13] This form of taxation ensures the wealthy pay their fair share while offsetting the regressive nature of other taxes like the sales tax and to a lesser degree the property tax, which consume a greater share of income for lower earners. Without the income tax, states must disproportionately rely on other taxation methods. Texas is second in the nation for its reliance on the property, where it accounts for 47% of

[11] Office of Rep. Paul Seaton, History of Alaska Individual Income Tax. NOTE: Some states such as Arizona have made their graduated income tax with multiple tax brackets into a flat income tax with one single tax rate. No state has eliminated all personal income tax brackets since Alaska in 1980.

[12] Who Pays? 7th Edition. Institute on Taxation and Economic Policy. January 2024.

[13] 29 states plus Washington D.C. have a graduated-rate income tax. 12 states tax personal income at a flat rate. Nine states do not tax personal income, although New Hampshire taxes income from interest and dividends and Washington taxes income from capital gains, both at flat rates. Andrey Yushkov, State Individual Income Tax Rates and Brackets, 2024. Tax Foundation. February 20, 2024.

state and local tax revenue. No state depends on the sales tax like Tennessee, where their 7% state sales tax rate accounts for 61.5% of total tax revenue. Florida also heavily relies on the property and sales taxes, accounting for 43.4% and 50.6% of their tax revenue, respectively.[14]

If these revenue sources prove to be inadequate, states make up for it through reduced public services. A generation of income tax cuts has prevented the Ohio state government from adequately responding to growing challenges Ohioans face. From unaffordable costs of higher education, to an unsustainable childcare market, everyday Ohioans continue to suffer from the abdication of duty from our elected officials. These private markets are failing us. When they do, government needs to have the resources to protect the welfare of their citizens. The answer simply cannot be to double down on the same policy choices that resulted in these failures in the first place.

Should lawmakers enact this dangerous income tax repeal, the inequality in Ohio's tax system will only be exacerbated. The personal income tax is the state's only tax that takes into consideration one's ability to pay and, as a progressive form of taxation, the income tax rate increases as your income does. This ensures higher income individuals pay their fair share in taxes while offsetting the regressive nature of other taxes, such as the sales tax, which consume a higher share of income for lower earning Ohioans.

Conclusion

Ohioans deserve an equitable tax system that supports the public goods and services that enable all of us to thrive. Unfortunately, thanks to a generation of cuts to the state personal income tax that mostly benefited the rich, that is not the system we have today. Our lawmakers now propose doubling down on this policy failure by fully eliminating the income tax. This is simply the wrong policy for Ohioans.

Two decades of income tax cuts has left the state unable to fully address issues such affordable childcare, education, and housing. Should the state eliminate over $11 billion in tax revenue, our government will fail to meet both these problems of today and the looming challenges of tomorrow.

[14] In the above source, see Appendix C: "Composition of State and Local Revenue by Source" for all states discussed.