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ISSUE BRIEF:

Decline of corporate income taxes in the United States and in Ohio
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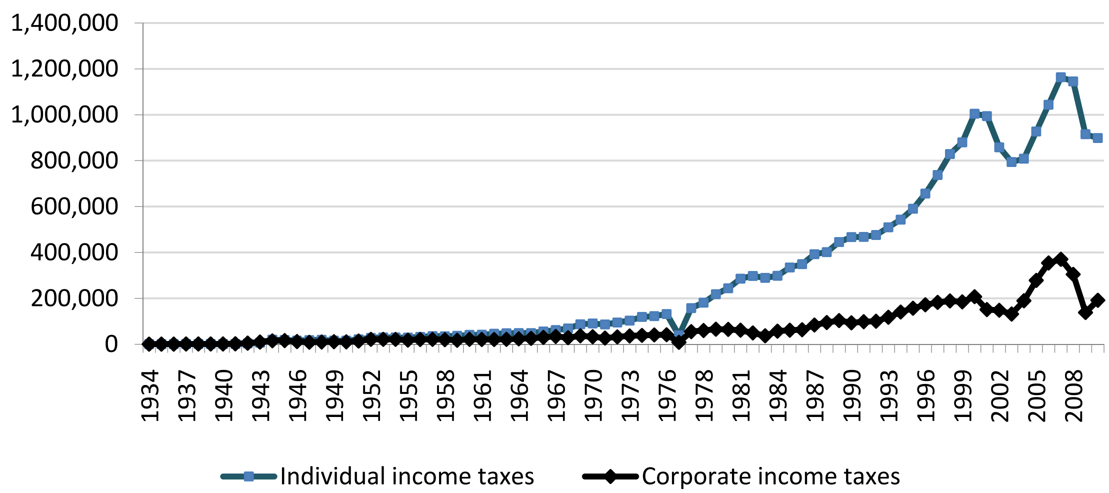
The share of revenues supporting education, infrastructure, health and well being of America's civic society has been supported more by individuals and families and less by corporations over time. This is true on both the national and the state level. As an epic struggle over fiscal resources emerges at all levels of government, this deserves a closer level of scrutiny. In this issue brief, Policy Matters Ohio looks at trends on the national and state level and gives recommendations for turning this trend around at the state level.

Figure 1: Comparison of individual and corporate income tax collections at the federal level, 1934-1912 (estimated; millions of dollars, not adjusted for inflation)



Source: http://nationalpriorities.org/en/resources/federal-budget-101/budget-briefs/federal-revenues/
http://www.whitehouse.gov/sites/default/files/omb/budget/fy2012/assets/hist02z1.xls (4/17/2011)

Figure 1 illustrates how the level of individual income tax collections diverge from corporate income tax collections in the 1970s, a trend that accelerated over time. Unadjusted, collections in individual income taxes shows the expansion of the economy in inflation. Corporate collections do not. Figure 2 compares individual and corporate income taxes as a share of total federal receipts over time, demonstrating the long-term decline of corporate contribution to public services.

Figure 2: Comparison of individual and corporate income tax collections as a share of total federal receipts, 1934-2012 (estimated) (millions of dollars, not adjusted for inflation)

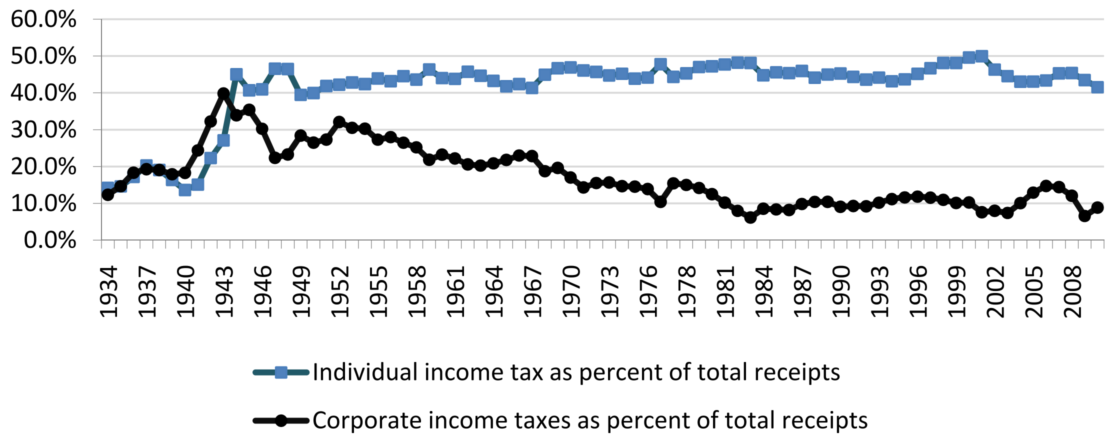


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Figure 2 illustrates that the source of revenue for public services had increasingly shifted from corporations to the individual. Between 1960 and 2010 corporate income taxes went from 23 percent of total federal revenues to 7 percent. Individual income taxes, on the other hand, have stayed relatively stable.[1]

According to the Brookings Institute, the United States has the second highest corporate tax rate of the 30 countries in the Organization of Economic Cooperation and Development (OECD). But because the United States has so many generous special tax preferences for businesses, it collects the fourth lowest corporate tax revenues as a share of GDP among all OECD countries.[2]

The story of General Electric's negative income tax, the subject of a New York Times article in March, drew new attention to inequities within the corporate tax structure over the past month. General Electric, the nation's largest company, reported worldwide profits of $14.2 billion in 2010, and said $5.1 billion of the total came from its operations in the United States, but it paid no taxes here; instead, it claimed a tax benefit of $3.2 billion.[3] This is not an uncommon story. A 2004 study of the corporate taxes on the wealthiest 275 domestic corporations in the United States found that almost a third of the firms studied paid zero or less taxes in one year of the three years between 2001 and 2003; that 28 firms

[1] National Priorities Project, Budget Briefs, Federal Revenues, at http://nationalpriorities.org/en/resources/federal-budget-101/budget-briefs/federal-revenues/, accessed 4/17/2011

[2] Jason Furman, *Corporate Taxes: In Need of reform.* The Brookings Institute, 10/27/2007. http://www.brookings.edu/opinions/2007/1027_corporate_taxes_furman.aspx, accessed 4/17/2011.

[3] David Kocieniewski, G.E.'s Strategies Let It Avoid Taxes Altogether, New York Times, March 24, 2011, http://www.nytimes.com/2011/03/25/business/economy/25tax.html?sq=Immelt%20taxes&st=cse&scp=4&pagewanted=all Accessed 4/17/2011.

enjoyed negative federal tax rates in all three years; and that GE was number one among the tax code winners. On the federal level, key loopholes include:[4]

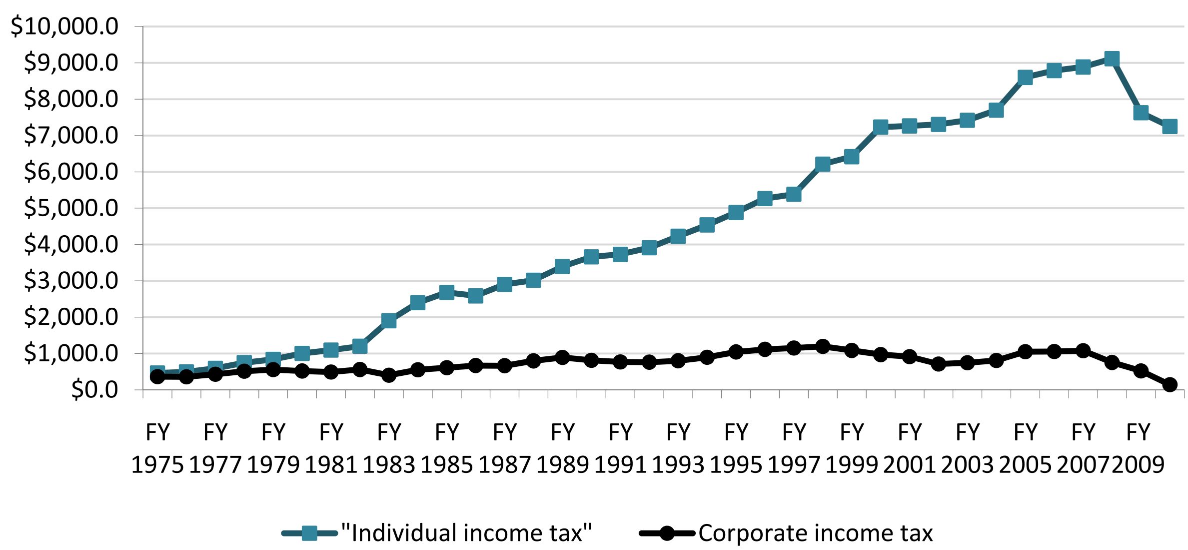
- Accelerated depreciation[5]
- Stock options for top executives
- Tax credits Offshore tax sheltering
- Weakening of the Alternative Minimum Tax for Corporations

Access to lawmakers through a variety of tools, extending from campaign finance to philanthropy of corporate foundations, enable corporations shape the tax code to their interest. The non-partisan Institute for Tax Policy suggests that in the absence of rational controls, tax departments like GE's become profit centers.[6] The profitability helps boost shareholder dividends, but not jobs – in the case of GE, since 2002, the company has eliminated a fifth of its work force in the United States while increasing overseas employment. In that time, G.E.'s accumulated offshore profits have risen to $92 billion from $15 billion.[7] Across the 275 companies studied by Institute for Taxation and Economic Policy in 2004, the average tax break was $175 million per company from 2001 to 2003, yet their investment in the United States declined by 15 percent in the same time frame.[8] Corporations seek tax breaks, but the expected return – domestic investment and jobs – does not always occur.

Corporate taxes in Ohio

Corporate taxes in Ohio, as in the rest of the nation, were low and got lower in the past decade. Corporate taxes have plunged due to the tax overhaul of 2005. Figure 3 illustrates the contrast between corporate income tax receipts and individual income tax receipts in the state of Ohio between 1976 and 2010.

Figure 3: Individual income and corporate income tax receipts funding the General Revenue Fund in Ohio between 1976 and 2010 (millions of dollars; not adjusted for inflation).



Source: Policy Matters Ohio based on data from Legislative Services Commission, Historical GRF Revenues

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[4] Robert McIntyre and T.D. Coo Nguyen, *Corporate Income Taxes in the Bush Years*, Institute on Taxation and Economic Policy, September 2004.

[5] A Bush administration tax cut for business with a value of $70.9 billion over 2001-2003; intended to spur investment, but total investment at the top 275 dropped by 12 percent between 2001 and 2002, and by another 3 percent the following year.

[6] Kocieniewski, Op.Cit.

[7] Kocieniewski, Op.Cit.

[8] McIntyre, Op.Ct., p.12

Individual income tax collections reflect inflation, but corporate tax collections remained flat over time. Yet consulting and accounting firms that ostensibly measure the 'business climate' based on taxes and unionization of the workforce blamed Ohio's business taxes and workers for long-term loss of well-paid manufacturing jobs. The source of distress is well documented: manufacturing job loss in Ohio's cities over the past decade has been staggering (Table 1). Politicians have been hard pressed for answers.

Table 1: Manufacturing job loss in Ohio cities over the past decade

Place	Manufacturing jobs, 2009	Manufacturing jobs, 1999	Percent change
Ohio	629,200	1,027,600	-38.8%
Akron MSA	37,900	59,300	-36.1%
Canton - Massillon MSA	25,400	45,000	-43.6%
Cincinnati - Middletown MSA	106,700	149,100	-28.4%
Cleveland - Elyria - Mentor MSA	118,200	196,500	-39.8%
Columbus MSA	66,100	99,300	-33.4%
Dayton MSA	39,000	78,900	-50.6%
Lima MSA	7,600	12,600	-39.7%
Mansfield MSA	9,700	16,700	-41.9%
Sandusky MSA	4,800	9,600	-50.0%
Springfield MSA	6,300	12,600	-50.0%
Steubenville-Weirton MSA	6,500	13,100	-50.4%
Toledo MSA	36,000	62,000	-41.9%
Youngstown - Warren - Boardman MSA	26,300	54,400	-51.7%

Source: Policy Matters Ohio based on US Department of Labor, Bureau of Labor Statistics, Current Employment Statistics (CES) survey; accessed through the Ohio Department of Jobs and Family Services Labor Market Information portal (Nonagricultural wage and salary jobs by place of work).

Too often, the remedy has been the 'supply side' economics of the 1970s, which was based on lowering costs of taxes and labor, an approach controversial to both Presidents Ronald Reagan, who shut down corporate tax breaks in his tax reform of 1986, and President George H. W. Bush, who called the tax cutting "Voodoo Economics." However, in the face of international trade agreements that did not protect American operations and workers, states increasingly went to war with each other using supply-side weapons of cutting taxes and workers' rights in an effort to lure factories.

The consequence of this was House Bill 66, which in 2005 overhauled the state's tax system, granting the largest tax cut of 70 years and laying the foundation for today's bitter budget battle. As part of that overhaul, the corporate income tax was phased out, making Ohio one of just four states without a tax on corporate profits, and a major corporate tax that supported local government, the tangible personal property tax, was also phased out. The legislature replaced these two taxes with a new tax on Ohio gross receipts, the Commercial Activity Tax (CAT). The personal income tax was also cut by 21 percent. Together with several other changes, these tax cuts are costing the state $2.1 billion in annual net revenue, according to the Ohio Department of Taxation.[9] As the state grapples with the budget today, Senate Bill 5, which curtails public workers' rights, emerges as the Administration's answers to draconian cuts to schools and local governments. Budgets are to be balanced on the backs of the workforce in a political climate that values low costs for business far more than fair pay and rights for working people. This is the low road of economic development. It's a road to nowhere.

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[9] Ohio Department of Taxation, "Fact Sheet: Tax Reform in Ohio," accessed 4/18/2011 at http://tax.ohio.gov/divisions/communications/news_releases/documents/Tax_reform_fact_sheet.pdf

Upon signing House Bill 66, Governor Taft declared, "This historic tax reform plan creates a new business climate that will generate jobs, grow our tax base to support education and all public services and allow Ohio workers to support their family and their community."[10] This premise did not prove to be true. State and local taxes are not a key determinant of state economic performance.[11] Since the tax overhaul of 2005, Ohio's private sector economy has continued to contract:

- Ohio's share of the nation's jobs has shrunk from 4.06% to 3.87%.
- Our share of manufacturing jobs has fallen from 5.7% to 5.35%.
- Ohio lost 353,100 nonfarm jobs and 182,300 manufacturing jobs.

Summary and recommendations for reversing the trend in Ohio

In Ohio and in the nation, corporate taxes have declined while other taxes to support the public infrastructure of everyday life have picked up the slack. Nationally, between 1960 and 2010 corporate income taxes went from 23 percent of total federal revenues to 7 percent. In Ohio, corporate taxes have declined from 40 percent of total receipts to 30% since the 1970s. Adam Smith, Ben Franklin and Thomas Jefferson all suggested those who benefitted the most from the system should pay the most to support the system. Our situation today is badly off track.

Ongoing corporate tax cuts are not creating the conditions for new job growth on the state or federal level. In Ohio, given the revenue crisis we face today, and the failure of the 2005 tax overhaul to achieve its stated goals, the 2005 overhaul should be reversed. The business tax cuts should be revisited, restoring revenue provided prior to the 2005 tax overhaul. This would still leave the business share well below where it was 30 years ago. Business taxes can be rebalanced with taxes on families to make the system more fair, adequate and stable. There are a number of ways in which this could be done. Examples include:

- Companies grossing up to $1 million annually pay only $150 in CAT tax – less than a family of four earning wages at the poverty line. This fee could be boosted.
- Loopholes undermined Ohio's corporate profits tax. It could be reinstated at a low but fair rate, without carve-outs.
- The General Assembly eliminated a trigger mechanism that ensured the CAT would make up localities' revenue losses. That mechanism could be reinstated or the CAT rate increased.

Ohio's General Assembly has many options for addressing the budget shortfall. Balancing business taxes with taxes on working families is an important part of the solution. Other solutions include a review of the $7 billion in tax loopholes throughout Ohio's tax code and elimination of those that do not boost the economy. Ohio provides a tax loophole for lobbying and for timeshares in private aircraft. At a time that aid to help keep foster children with relatives is eliminated; while child and senior protective services are cut; when the Governor's Director for education says 50 children in a classroom is acceptable – this is a time that loopholes for time shares in private aircraft should be ended. In fact, all loopholes could be cut by 10 percent and raise hundreds of millions of dollars so we have less destruction of jobs and services and our civic economy.

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[10] Gongwer News Service. *Ohio Report.* "Taft signs $51.25 billion biennium budget." Volume #74, Report #129. June 30, 2005.

[11] South Dakota, with no income tax and the lowest overall state & local taxes in the country (as a share of personal income), had the 2nd lowest unemployment rate in the country in June, 2010. North Dakota, a state with an income tax and the 5th highest overall tax levels, had the lowest unemployment rate. It doesn't take an economist to see that the similar economies of the Dakotas have more to do with a strong economy than tax structure.

America faces a crisis of paying for the services people need to keep our country running, with safe roads and bridges, efficient ports, safe credit markets, good schools and a healthy workforce. It is time to recognize our crisis is one of revenues and to make corporations pay their fair share.