

The 2005 Tax Overhaul, Business and Ohio's Economy

Legislative briefing

February 19, 2009

--How has Ohio's economy responded to the 2005 tax overhaul?

--What has the business-tax revamp produced?

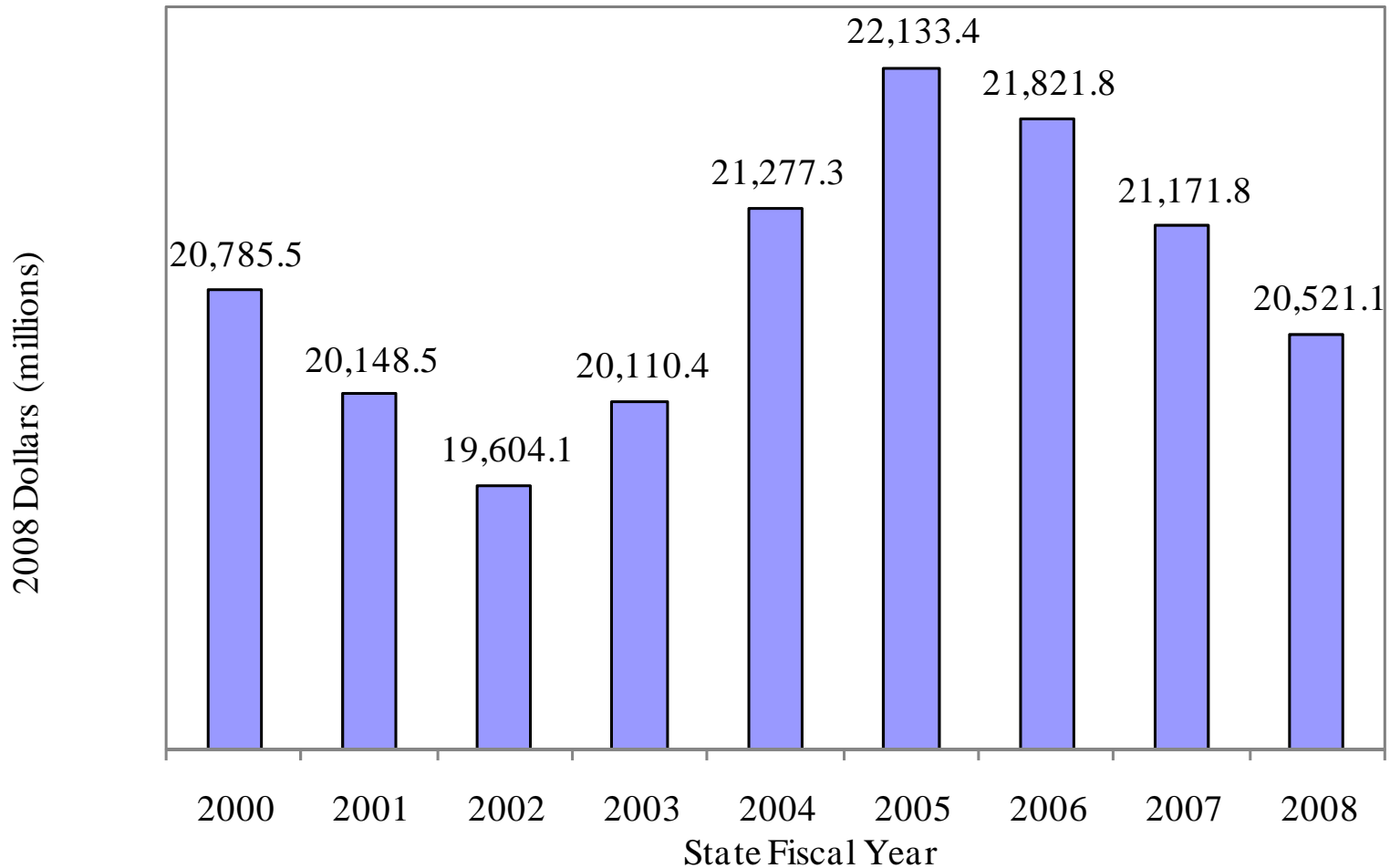
The 2005 Tax Overhaul and Ohio's Economy

Our baseline for evaluating the tax changes is Ohio's relative performance with respect to the nation and nearby states

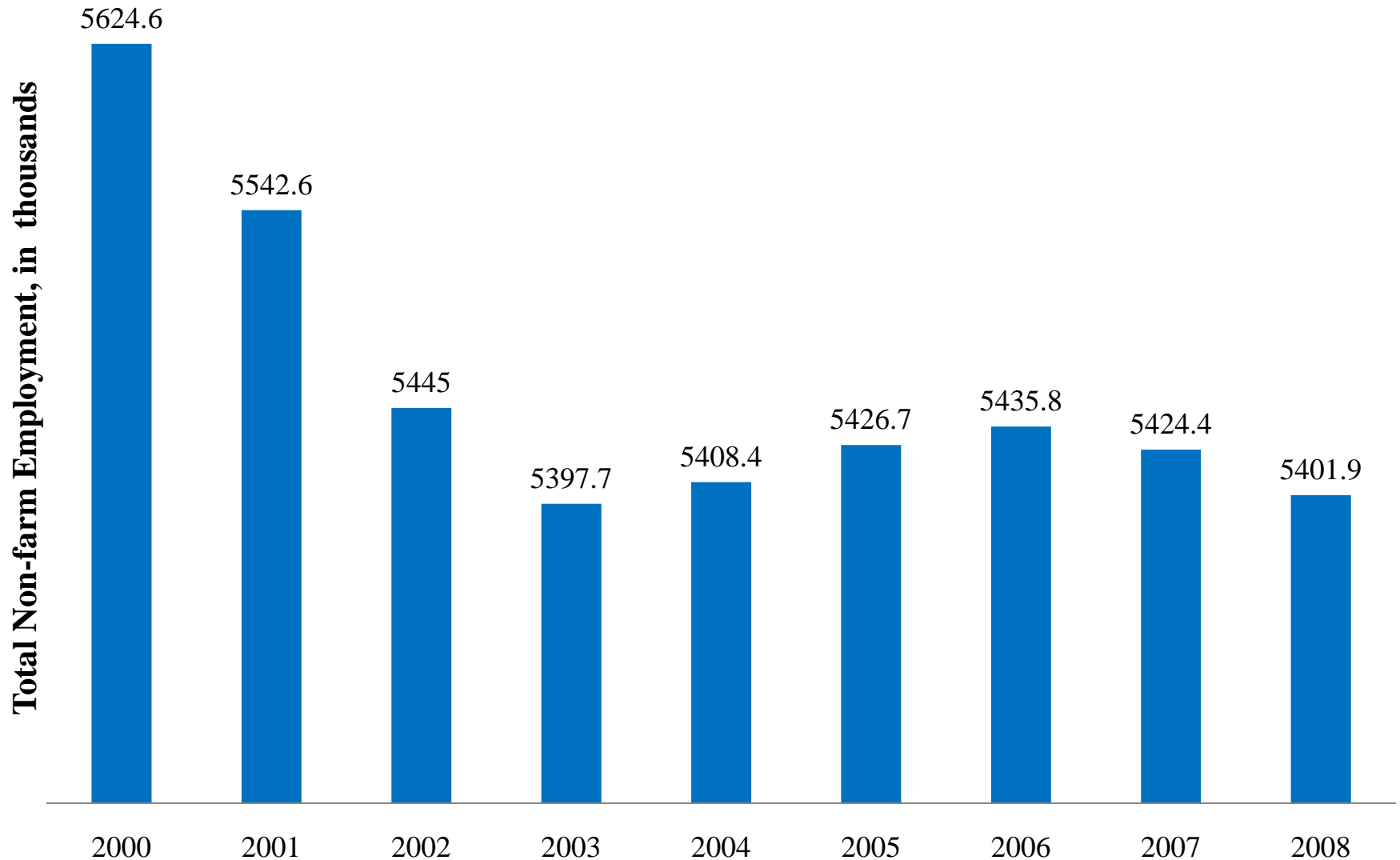
Before the recession, Ohio's economy failed to close the gap or even lost ground relative to the nation on important indicators:

- Employment
- Economic output
- Productivity
- Personal income
- Unemployment rates

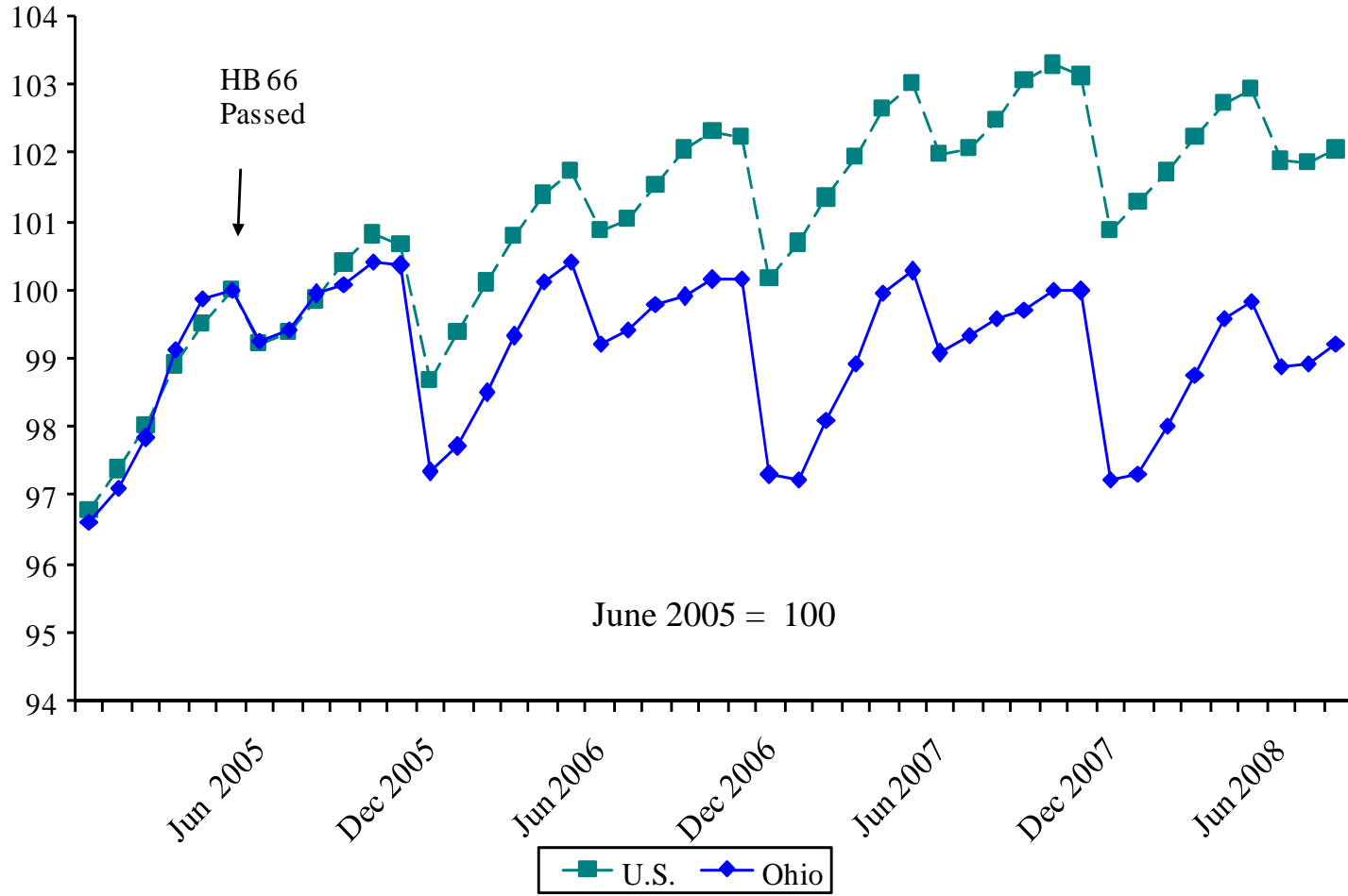
Inflation-adjusted State GRF Tax and Lottery Profit Revenue,
FY 2000-08



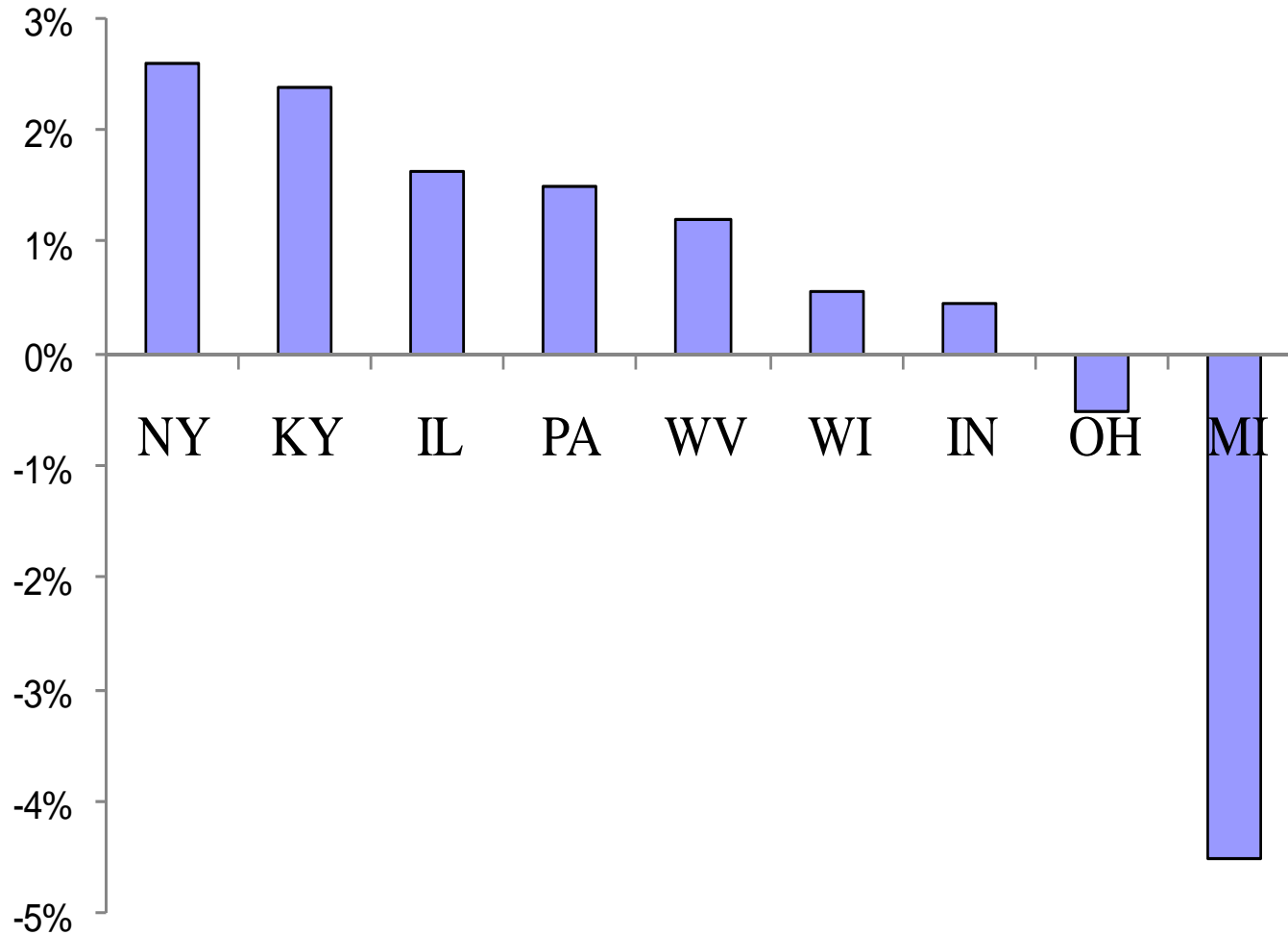
Ohio Average Annual Employment, 2000 - 2008



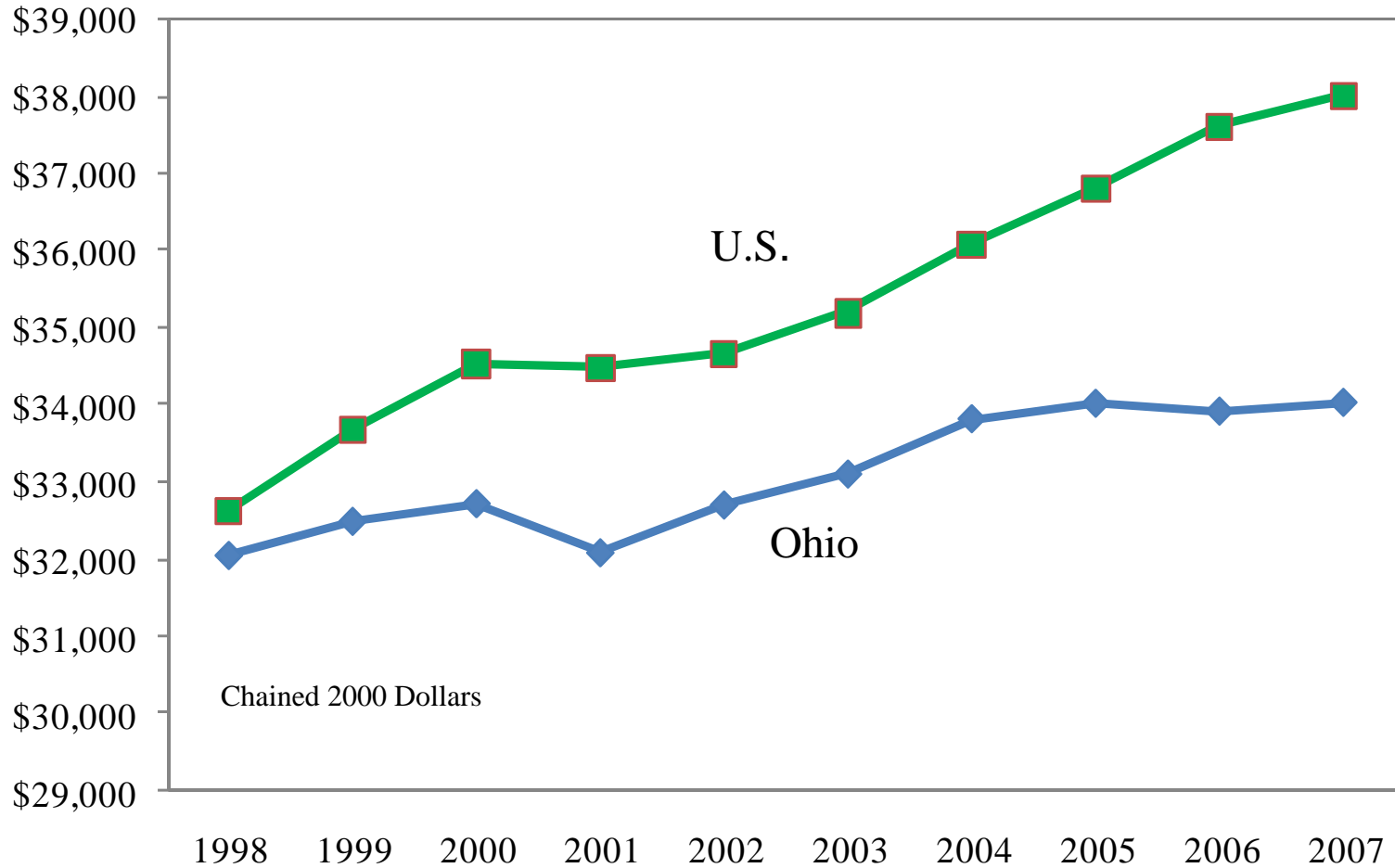
Index Comparison of Ohio and U.S. Total Employment, 2005 – September 2008



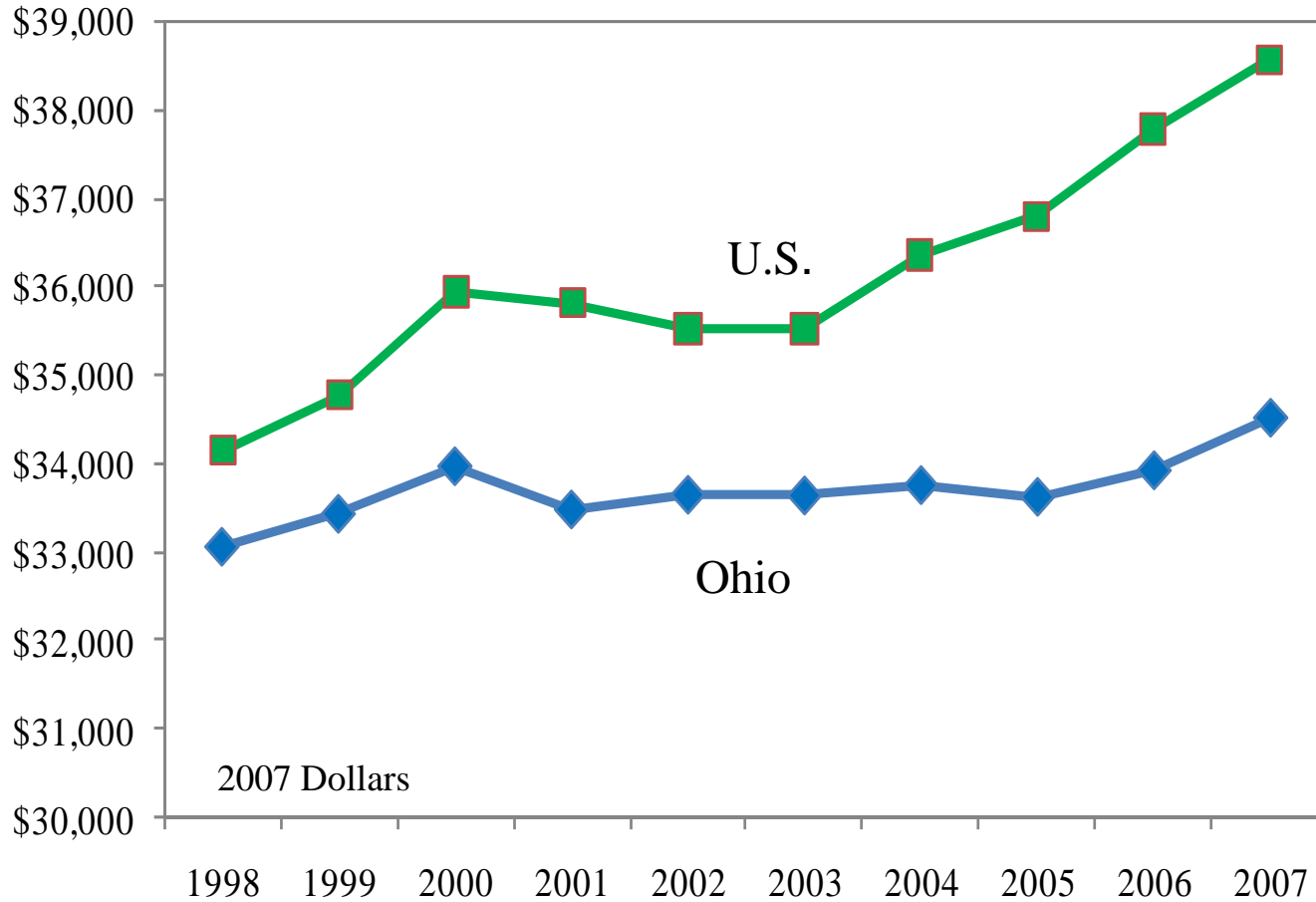
Three-year Change in Total Employment in Ohio
and Nearby States, 3Q 2005 - 2008



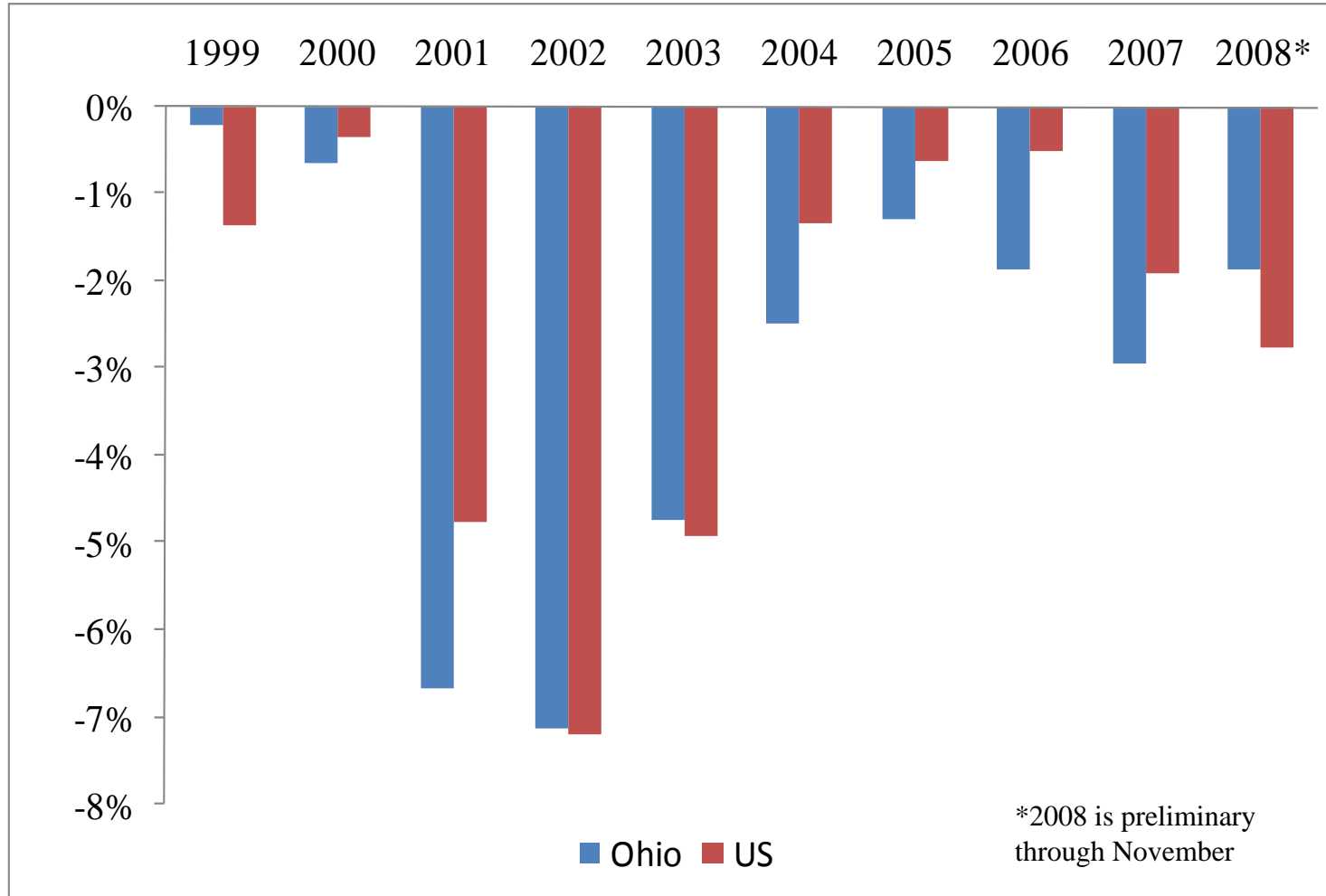
Ohio and U.S. Real GDP per capita, 1998 - 2007



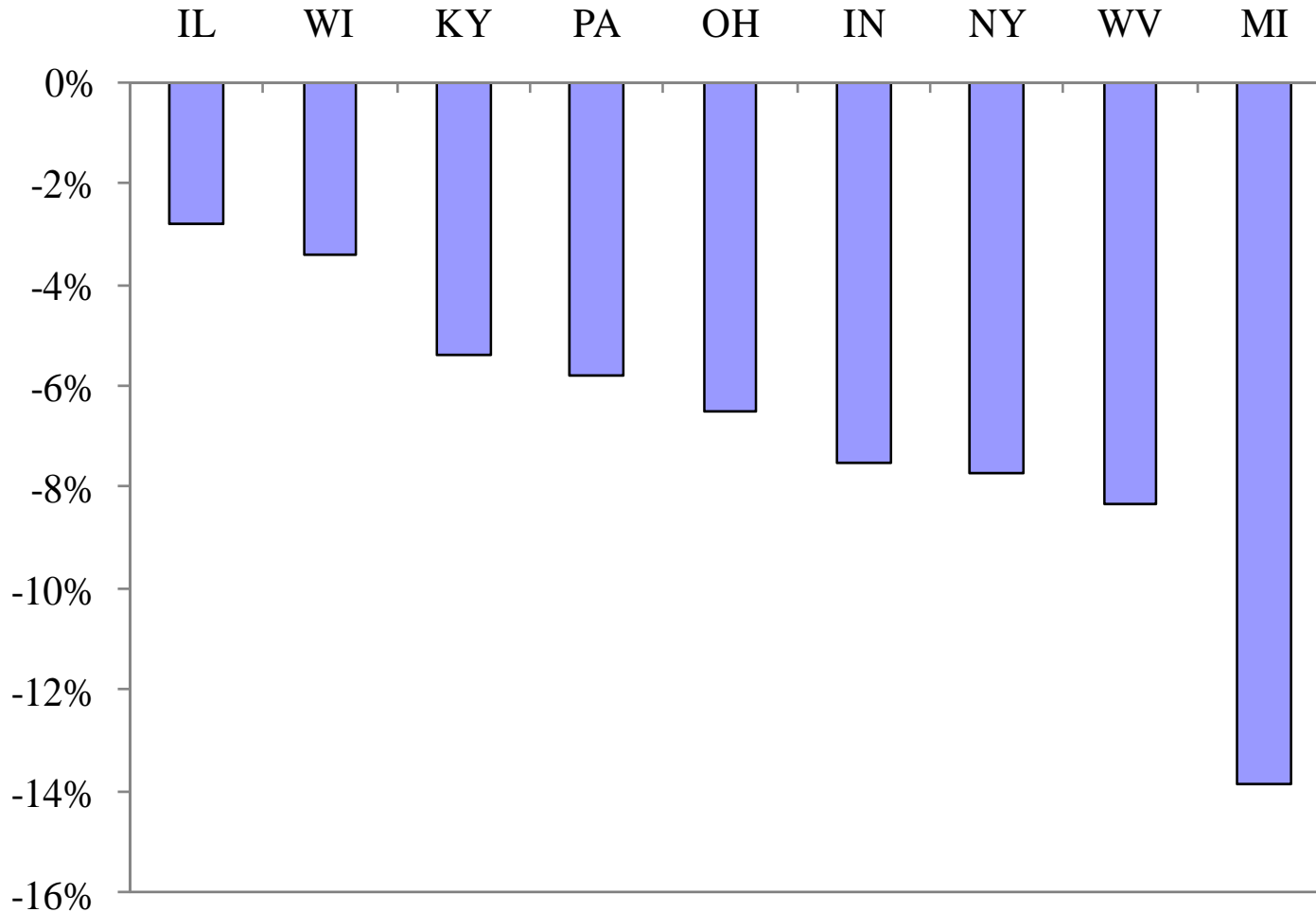
Ohio and U.S. Real Personal Income per capita,
1998 - 2007



Annual Change in Ohio and U.S. Manufacturing Employment, 1999- 2008

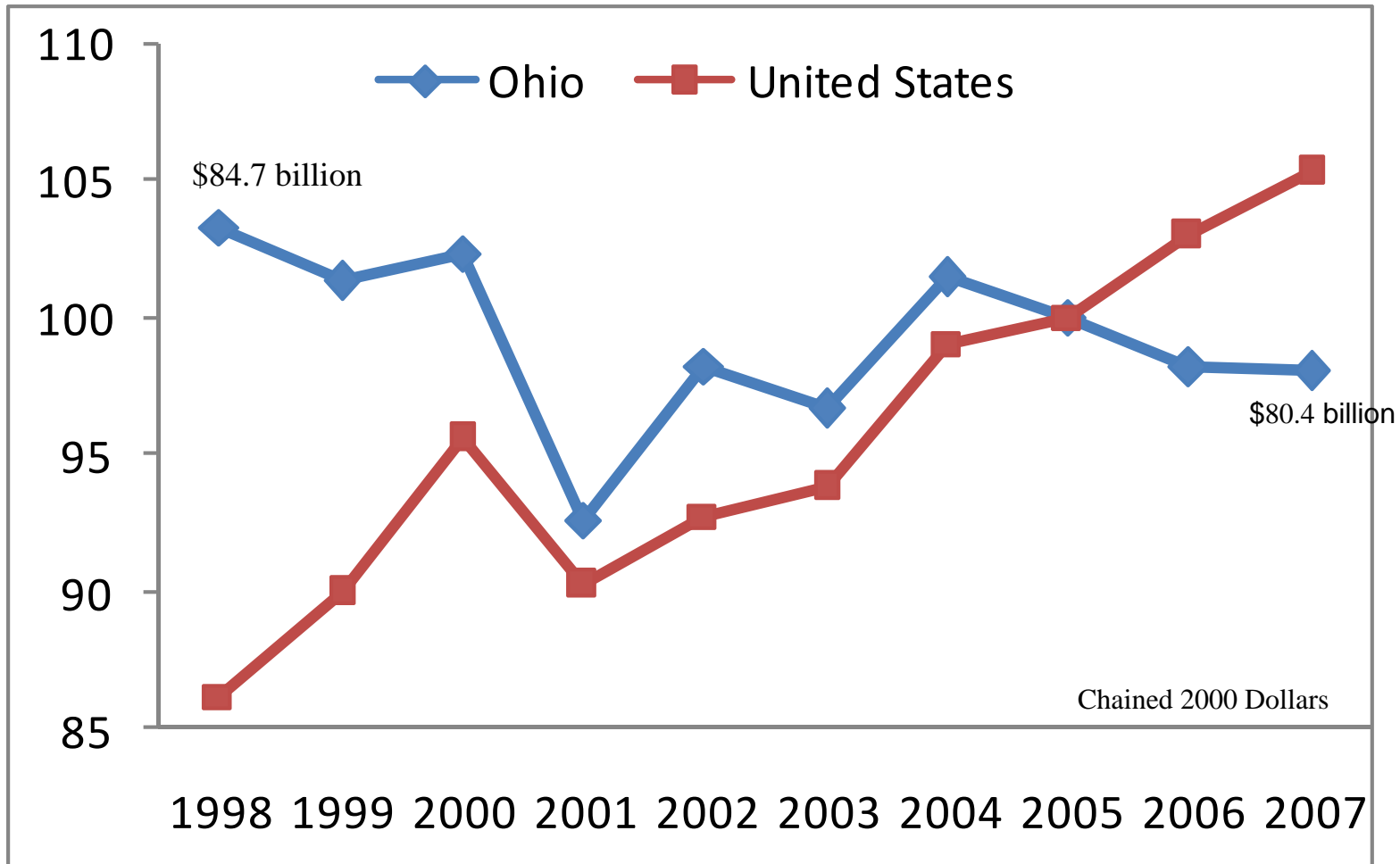


Three-year Change in Manufacturing Employment, Ohio and nearby states, 3Q 2005 – 2008



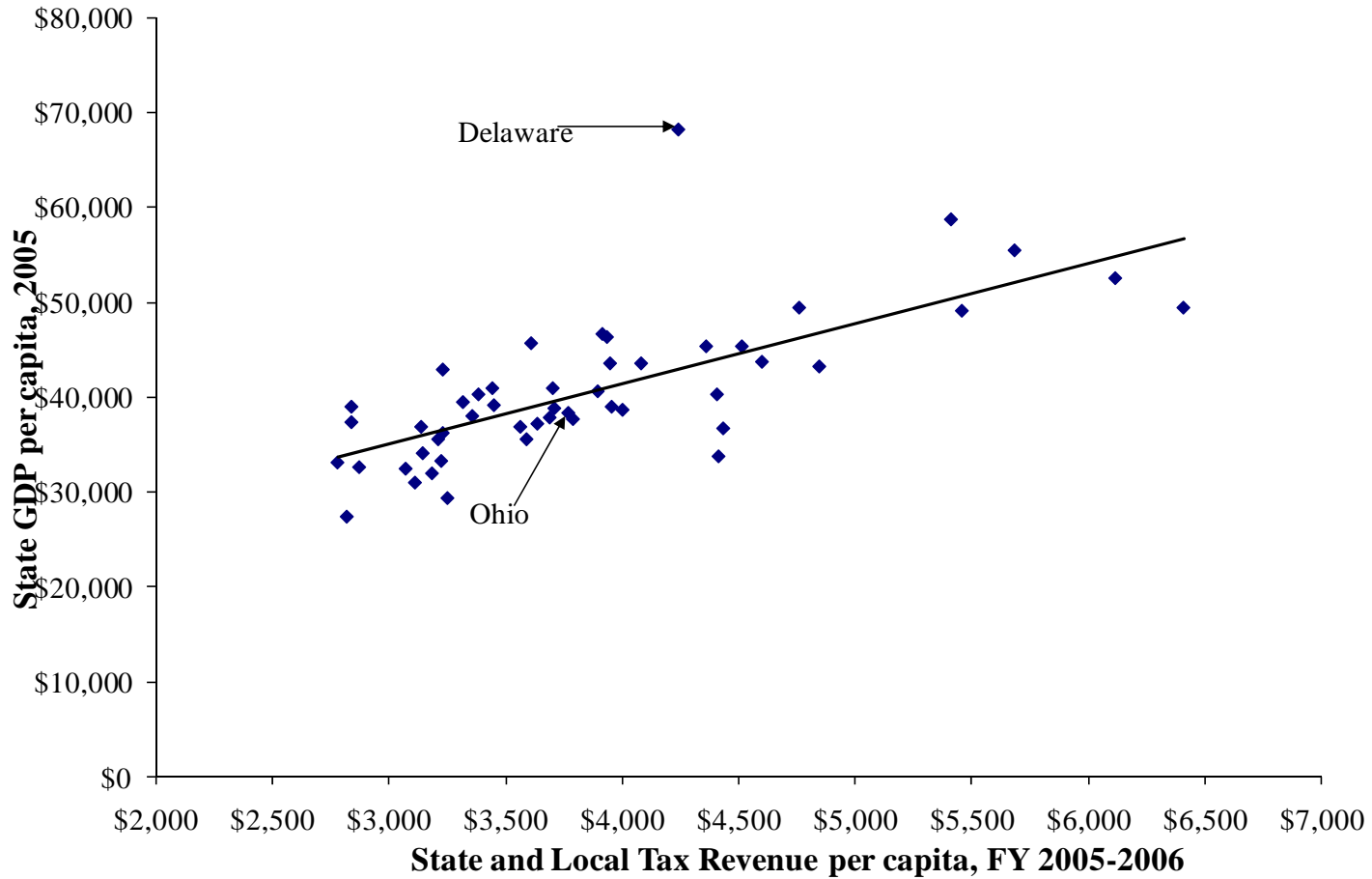
POLICY MATTERS OHIO

Index Comparison of Real Manufacturing GDP, Ohio and U.S.

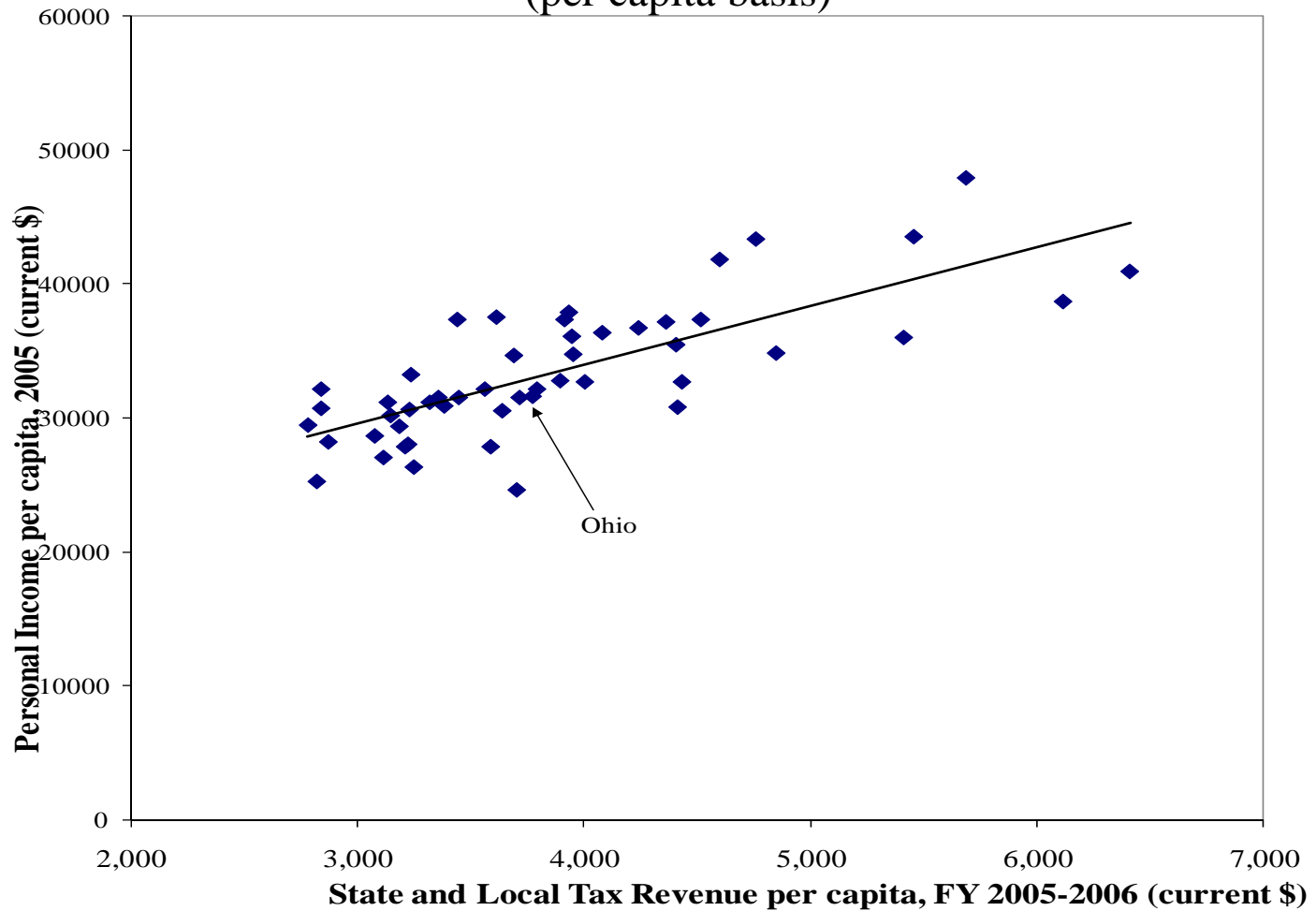


2005 Base Year = 100

State and Local Tax Revenue vs. State GDP 2005
(per capita basis)



State and Local Tax Revenue vs. Personal Income 2005
(per capita basis)



Conclusions

- The tax overhaul did not produce expected results to date and we cannot assume that it will in the future.
- The HB 66 framework impedes the state's ability to respond to the economic crisis.

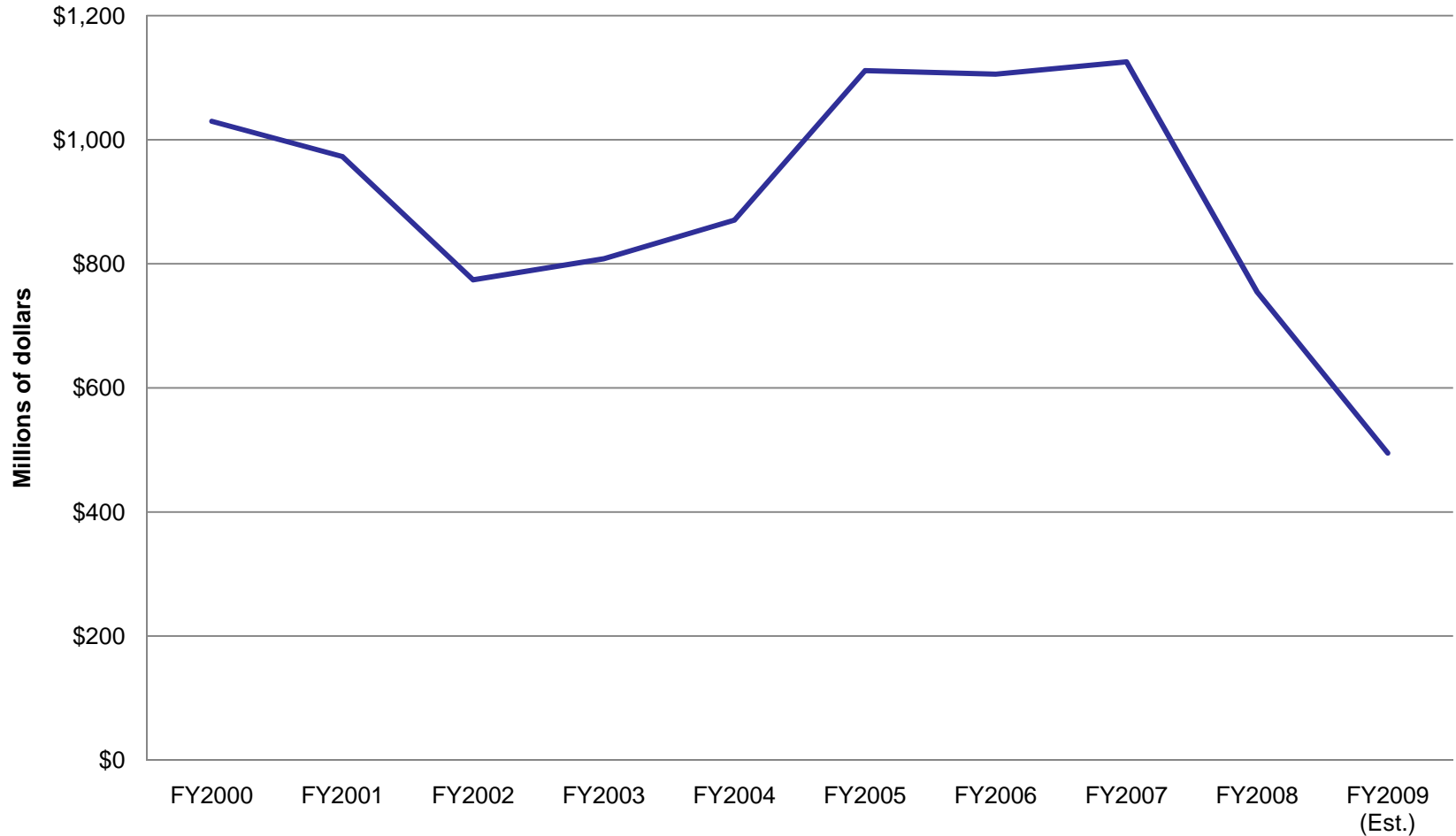
Conclusions - 2

- There is no direct relationship between tax rates and economic performance.
- Public services that maintain the quality of life and support critical economic development goals also impact the business climate.

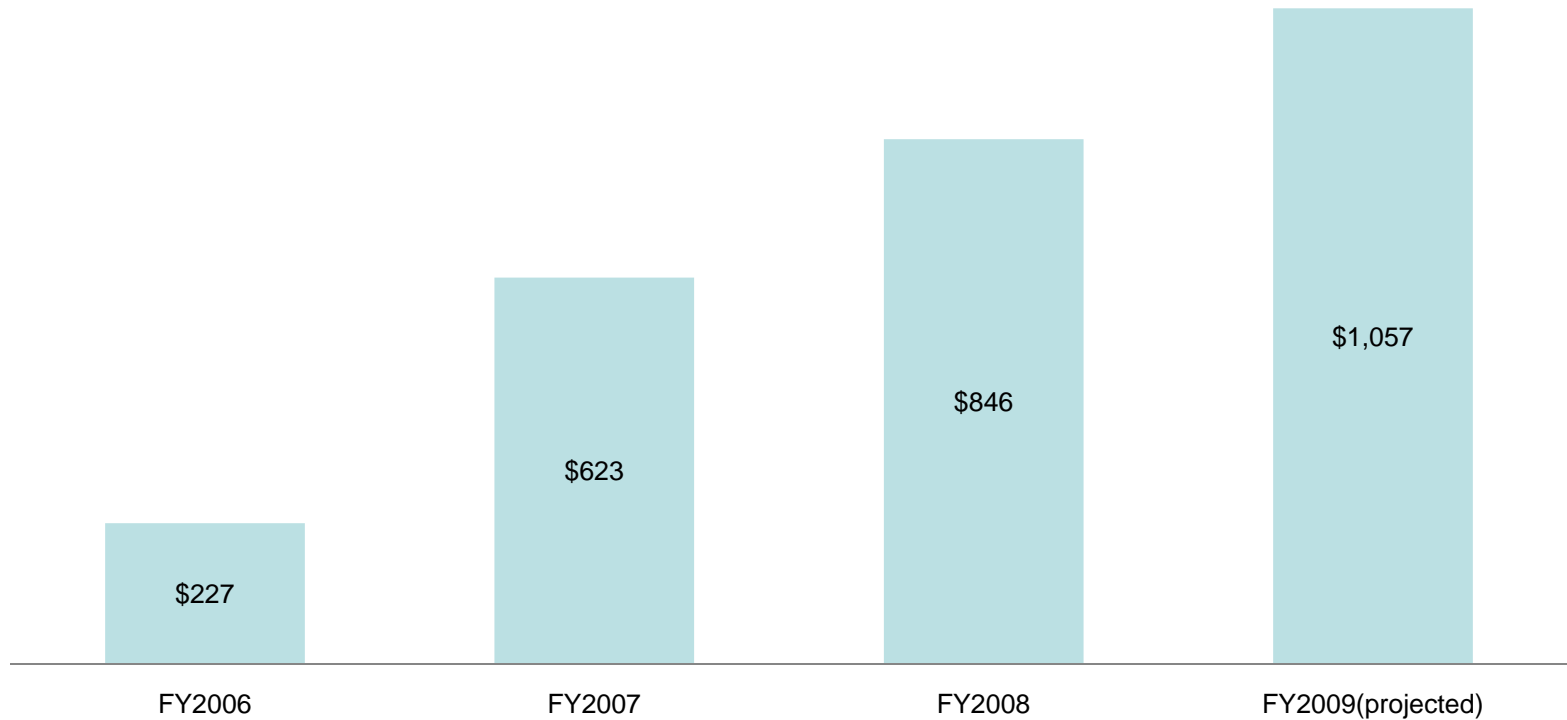
*Business Tax Revamp:
A Deficit in the Making*

- Phase-out of Corporate Franchise Tax, Ohio's corporate income tax
- Phase-out of Tangible Personal Property Tax, a local tax on machinery, equipment, inventory, furniture and fixtures
- Creation of Commercial Activity Tax on Ohio gross receipts

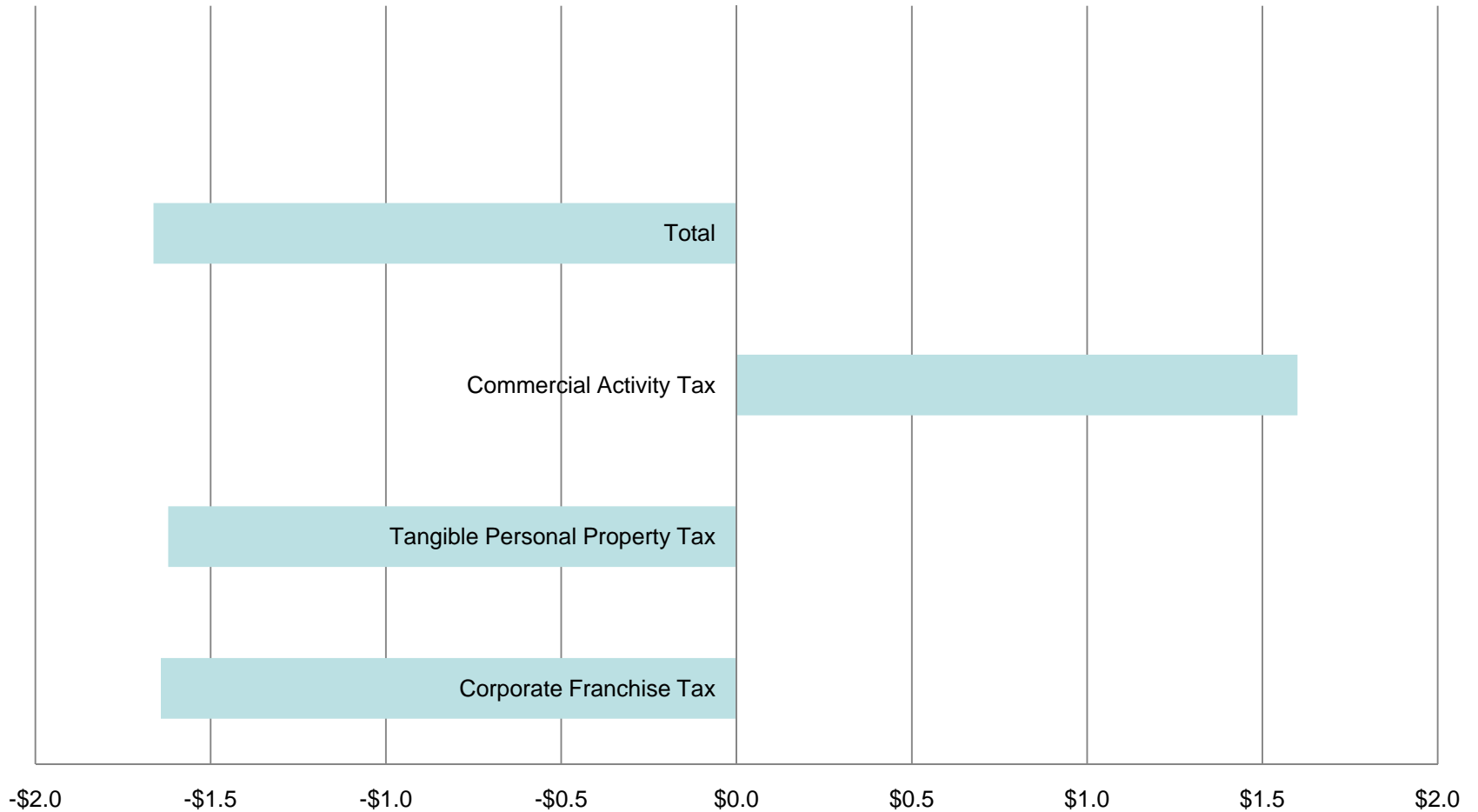
Corporate Franchise Tax Revenues, All Funds, Fiscal Years



Estimated Savings for Companies from Corporate Franchise Tax Cuts (millions of dollars)



Estimated FY10 Revenue Change under HB 66, in billions of dollars



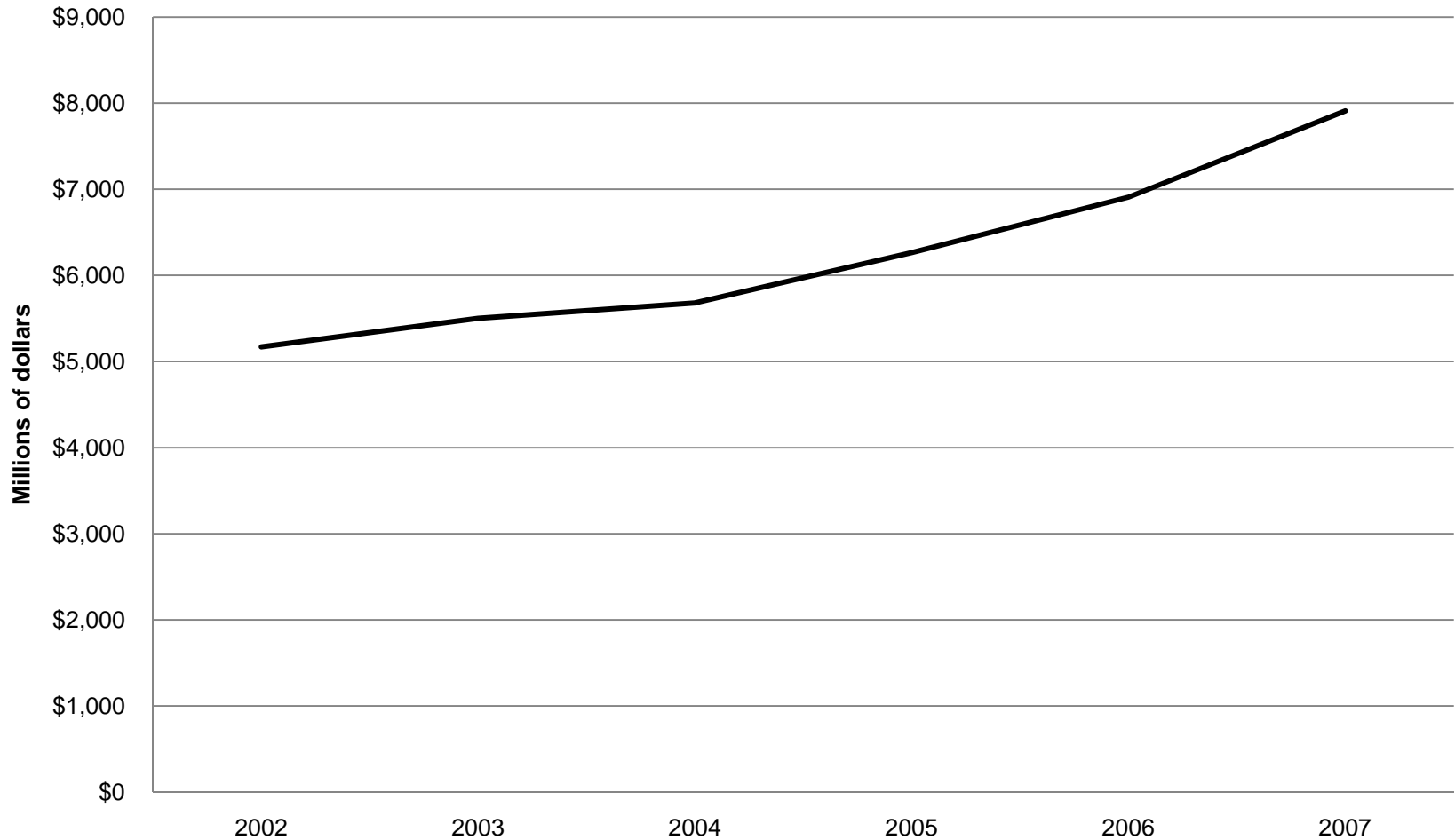
The business share of state and local taxes

- In a study supported by the Ohio Manufacturers Association, Prof. Ned Hill found that the business share fell from 39.6% to 28.9% between 1976 and 1999.
- Policy Matters Ohio finds that it has fallen since then, including a modest decline since HB 66.

Commercial Activity Tax

- A broad tax covering far more taxpayers
- 86% paid by companies with Ohio addresses, but hard to tell how much paid by Ohio operations
- Manufacturers are major beneficiaries, though they pay the largest share of CAT
- Most companies pay very little
- Significant exemptions and credits

Assessed Valuation of Real Property Tax Abatements, Tax Years



Threats to the CAT

- Downward trigger
- Lawsuits

Income-Tax Rate Cuts

Annual Tax Reductions for
Ohio Families (rounded):

- Top 1% -- \$10,300 or 1.2%
of income
- Middle 20% -- \$190 or 0.5%
of income

Income Tax Rate Cuts - 2

- Over 70 percent of gain goes to top 20 percent of income earners
- Annual Lost Revenue – \$2.2 billion

Recommendations

- Restore income-tax rate on income over \$200,000 to 7.5%
- Restore other income-tax rates to 2007 levels
- Establish a state earned income tax credit at 5% of the federal level

Net revenue impact: More than \$1 billion/yr

Recommendations - 2

- Limit tax breaks, e.g. means-test the homestead exemption. Total: Up to \$270 million a year
- Retain and strengthen the franchise tax: About \$1 billion a year

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