Policy Matters Ohio

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Testimony of Hannah Halbert, Policy Liaison, Policy Matters Ohio
before the House Ways & Means Committee on HB 98, March 30, 2011

Chairman Beck, Ranking Member Letson and members of the Ways & Means Committee, thank you for the opportunity to testify today. Policy Matters Ohio is a nonprofit, nonpartisan organization conducting research on issues facing working families in Ohio.

We asked the Institute on Taxation and Economic Policy, a Washington, D.C., research group, to examine House Bill 98. ITEP has a computer model of the tax system of all 50 states. Its analysis of HB 98 covered Ohio residents age 71 and over, a slightly smaller group than those at least 70½.

ITEP found that half the gain would go to the less than 1 percent of older taxpayers with annual income of $321,000 or higher. Altogether, those taxpayers would each average a gain of more than $3,000 a year. Nearly two-thirds of Ohio residents 71 and over would get no benefit from this bill, and among those who did, they would be heavily concentrated among the most affluent. Even those seniors with incomes between $75,000 and $136,000 would receive on average just an $83 cut in annual income taxes. The following table describes how the gains would be broken out by income group:

Analysis of HB 98 (Optional 1% on Unearned Income for Those Over 70)

Ohio Residents, 2010 Income Levels							
Income Range	Less Than $18,000	$18,000 - $32,000	$32,000 - $49,000	$49,000 - $75,000	$75,000 - $136,000	$136,000 - $321,000	$321,000 Or More
Average Income in Group	$11,000	$24,000	$40,000	$61,000	$96,000	$194,000	$880,000
Tax Change as % of Income	—	–0.0%	–0.0%	–0.0%	–0.1%	–0.1%	–0.3%
Average Tax Change	$ -	$ (0)	$ (3)	$ (28)	$ (83)	$ (264)	$ (3,012)
Percent of Total Tax Change $	—	0%	1%	10%	21%	18%	51%

SOURCE: Institute on Taxation and Economic Policy Microsimulation Tax Model, March 2011

For those older Ohioans with the lowest incomes, this would not be advantageous, since they pay a lower rate than that now. However, for those paying the top rate of 5.925 percent on income over $201,800, this would be a windfall.

House Bill 98 would cost about $325 million in lost annual tax revenue to the state, according to the ITEP analysis. Though that could slightly understate the total since it does not cover those between 70½ and 71, the Legislative Service Commission previously estimated the revenue loss at roughly $360 million. Even if this does not impact the FY12-13 biennium, it tears a major hole in budgets to come.

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House Bill 98 also would add lines to the income-tax form and complicate the job of filling it out. That is because seniors would need to divide up their income between earned and unearned income, and figure their tax two different ways. Exemptions would be subtracted first from earned income, and if the exemption amount exceeds earned income, the excess is to be subtracted from unearned income. Individuals choosing the 1 percent rate on unearned income could not subtract the state's retirement income credit of up to $200.

Older Ohioans already receive some benefits under the Ohio income tax. It does not cover Social Security benefits, and besides the retirement income credit, the state also offers a $50 senior citizen credit.

Much of the unearned income covered under the bill consists of capital gains. However, there is little connection between lower capital gains taxes and economic growth at the national level. [1]

Cutting capital gains taxes at the state level as in HB 98 is especially unlikely to improve economic growth. That's because such taxes apply to investments whether they are made in the state where the investor lives or not. If Ohio offers a lower tax rate on capital gains, Ohio investors get the same tax cut whether they invest in Ohio or anywhere else. They will invest where they can get the highest return, and that won't be affected by a lower-capital gains tax in Ohio.

Affluent Americans are actually less likely to live in states without an income tax than in states with such a tax. According to data from the Internal Revenue Service, a slightly smaller share of all taxpayers with income over $200,000 in 2008 lived in states without income taxes than the share of all taxpayers in those states. The change has been small, but this disparity grew between 2005 and 2008—meaning the most affluent taxpayers were more likely to live in states with an income tax. This does not support the idea that affluent taxpayers are flocking to states without income taxes.

In addition, because of the interaction of the federal tax code, a cut in the state tax rate on unearned income would lead to higher federal tax bills and a greater flow of income out of the state to the federal government. It would reduce the deductions that can be itemized on federal tax returns.

Ohio already has tested the theory that providing tax cuts for the affluent will lead to stronger economic growth, and found it wanting. In 2005, the General Assembly approved a tax overhaul that reduced income-tax rates by 21 percent. Because Ohio has a graduated income tax, much of this gain went to the wealthiest Ohioans. Those in the top 1 percent of the income spectrum on average are seeing a $10,000 annual tax cut, according to a previous ITEP analysis, and more than 40 percent of the total reduction went to those making at least $135,000 a year.

However, Ohio's economy has continued to lose ground to the rest of the country. We have a smaller share of the nation's jobs and manufacturing jobs. Meanwhile, revenue available for needed public services has been lost.

For these reasons, we believe House Bill 98 will not serve the interests of Ohio.

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[1] See, for instance, Burman, Leonard and Kravitz, Troy, "Capital Gains Tax Rates, Stock Markets and Growth," *Tax Notes*, November 7, 2005, cited in Institute on Taxation and Economic Policy, "A Capital Idea," January 2011, p. 7. Also see Ettlinger, Michael and Irons, John, "Take a Walk on the Supply Side," Center for American Progress and Economic Policy Institute, Washington, D.C., September 2008.