Policy Matters Ohio

Tax Policy

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Testimony to the Senate Ways & Means Committee on House Bill 59 proposed tax provisions

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Good afternoon, Chairman Schaffer, Vice-Chair Peterson, Ranking Member Tavares and members of the committee. My name is Wendy Patton and I am senior project director at Policy Matters Ohio, a nonprofit, nonpartisan organization with the mission of creating a more prosperous, equitable, sustainable and inclusive Ohio. Thank you for the opportunity to testify today regarding House Bill 59. I am testifying today on behalf of our research director, Zach Schiller.

We have only just learned of the new tax provisions being put forward, and so our analysis of them is necessarily limited. Adding this many significant tax changes into the budget bill at this late date does not allow for either the proper study or debate that should accompany major changes in the tax code.

Simply put, the new provisions as announced will shift the tax load to low- and middle-income Ohioans from upper-income residents who are in a better position to pay. Ohio's overall state and local tax system - comprised of sales taxes, property taxes, income and other taxes - this overall system already leans heavily on the bottom fifth of tax filers. Those at the bottom of the income scale pay on average 11.6 percent of their income in state and local taxes, while the top 1 percent pay just 8.1 percent. The structure of Ohio's income tax helps balance that inequity. Reducing the income tax and replacing a considerable portion of the revenue with a sales-tax increase amounts to a direct shift in who pays taxes in Ohio. Rather than raising the rate of the sales tax, the base should be broadened, so that it covers what is sold in today's economy.

The proposed income-tax cuts reduce Ohio's ability to invest in its people. We do not support preschool education for nearly enough of our children, while college remains unaffordable for many. Too many K-12 schools have cut back on courses and teachers. Local governments struggle to provide services. Basic human services, from foodbanks to protection of our elderly, are insufficient.

We have testified previously on the prior proposal to exempt half of business income from passthrough entities, up to $750,000. Lowering that cap to $250,000 is a step in the right direction, as it reduces the amount that wealthy passive investors, partners in law firms and others will obtain through this exemption. But this exemption is fundamentally flawed. Most of those who will benefit do not employ anyone besides their owner now, and are unlikely to hire new workers merely because they get a tax cut.

Moreover, capping this tax break at a lower level means the maximum amount available under it will be less than $7,000 a year. Most owners will get a fraction of that. At the same time, this creates a giant new tax break, worth more than half a billion dollars a year, that far outweighs all of the smaller loopholes closed in this legislation. This new tax break also creates a new avenue for tax avoidance.

We have supported and testified earlier in support of a refundable state Earned Income Tax Credit. As its title states, an EITC is only available to families that work. This proposal for a nonrefundable credit will dramatically limit its value. Only three of the twenty-four states with an EITC program have a nonrefundable credit. Since the overall tax proposal would increase the sales tax rate, eliminate the credit for those making $10,000 a year or less and repeal the $20 personal exemption credit, the benefit of the new EITC is further reduced. Some individuals and families will do worse under the new plan. No one should end up worse off as a result of these tax changes. We need a stronger, refundable EITC.

There are other positive elements to this proposal. Means-testing of the homestead exemption will save the state money spent for those who don't need it, though this change should not extend only to future seniors. Levying taxes on digital products makes sense, as does collecting sales tax already due on Internet purchases.

However, this bill creates new tax breaks, for aerospace companies, for-profit grain handlers and some fraternal organizations, among others. It expands a variety of existing tax breaks, from a special-interest local sales-tax break to the Job Retention Tax Credit. Nor is any provision made to review the loopholes in the tax code. HB 59 represents another foregone opportunity to truly examine our $7 billion in annual tax expenditures.

Local governments are still suffering from the cuts in funding in the last state budget, which have not been reversed in this one. But those that are then faced with raising local levies to make up the difference and continue providing needed services will face a new obstacle with the proposal to end state reimbursement for property tax rollbacks involving new and replacement levies.

Cutting income taxes is unlikely to spark the state's economy. Ohio approved rate cuts in 2005 that were twice the size of the 10 percent reduction being put forward and they have not resulted in better economic performance. A report this week from the Center on Budget and Policy Priorities examining the academic literature noted "there is no clear research evidence that lower taxes help state economies grow" (see Michael Mazerov, "Academic Research Lacks Consensus on the Impact of State Tax Cuts on Economic Growth," Center on Budget and Policy Priorities, June 17, 2013, at http://www.cbpp.org/cms/index.cfm?fa=view&id=3975).

Thank you for allowing me to testify on this legislation. I am happy to answer any questions that you or any of the other members of the committee may have.

Policy Matters Ohio is a nonprofit, non-partisan research institute with offices in Cleveland and Columbus.