Multiple Reports Show Economic Benefits of No State Income Tax are Significant

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State income taxes have been an issue through out the United States, especially here in Ohio for some time, however the calls for reform have gotten louder over the past year. One of the proposed reforms has been the elimination of the state personal income tax. Nine states (Alaska, Florida, Nevada, New Hampshire, South Dakota, Tennessee, Texas, Washington, Wyoming) already collect no personal income tax from their residents. Oklahoma, among other states, has recently considered joining those without a state income tax.

The Oklahoma Council of Public Affairs published a report by Dr. Arthur Laffer analyzing the impact elimination of the state income tax could have on the state.

In the report, Dr. Laffer proposes a gradual phaseout of the top marginal individual income tax rate to zero by 2022. The proposed phaseout is expected to give Oklahoma a boost in population and economically. According to the report, Oklahoma has seen gross state product growth of 51.81% and a 1.05% net domestic in-migration growth as a percentage of the population over the past ten years. The nine states with no personal income tax saw considerably higher gross state product growth, 58.54%, and net domestic in-migration, 4.12%. The report found the nine states with the highest personal income tax rate saw considerably lower growth in gross state product, 42.06%, and a loss of 1.91% in net domestic in-migration. Ohio did much worse than the average for high tax states with a gross state product growth of 24.8% and a loss of 3.1% in net domestic in-migration. The Ohio numbers are part of a larger trend dating back to the introduction of the state income tax in 1972. Since 1972, Ohio has seen its percentage of U.S. GDP fall by 2.14% and its percentage of the U.S. population fall by 1.51%.

While Oklahoma performs above the national average in both economic and population growth, Dr. Laffer argues they could do better with the proposed phaseout. According to the report, Oklahoma can expect to see $47.7 billion more in personal income and $53.4 billion more to state GDP by 2022 if the state personal income tax is phased out. Critics of Dr. Laffer's report point out that some high tax states have recently outperformed some of the lower tax states. Dr. Laffer responded that his proposal increases the likelihood of success and that, despite short term blips, low tax states have performed better than high tax states in the long term.

The Cato Institute pointed out similar trends on a national level using regression analysis. The Cato Institute report, which attempted to control for the so called regional advantages trumpeted by the Laffer critics, concluded

"Jurisdictions that imposed an income tax to generate a given level of revenue experienced lower rates of economic growth relative to jurisdictions that relied on alternative taxes to generate the same revenue."

The Maine Heritage Policy Center found similar trends when analyzing their own state income tax burden. According to the report, Maine, which has a top marginal income tax rate of 8.5%, "lost 11,468 people and $661,274,000 in income," as well as $87,004,000 in taxes, from 1995 to 2009. The Maine Heritage Policy Center found that much of the migration out of Maine has gone to states without an income tax.

The Pacific Research Institute also found similar results when analyzing California. On the positive side, the California report found that the state had an annual gross state product growth of 3.6% from 2003-2007, which puts it near the top compared to other states. On the negative side, average private sector employment growth from 2004-2008 was 0.8%, with only 74% of the workforce employed in the private sector over the same time period. California also saw a decrease of 0.6% in net domestic migration as percent of the population from 2004-2008, which compares unfavorably to other western states. The report observes, *“while California experienced a net outflow of more than one million residents over the last five years, Oregon and Washington together attracted more than 260,000 residents (net) while the other Southwest states attracted a net inflow of more than 904,000.”*

Ohio policymakers would be wise to consider the findings of Laffer, as well as other policy institutes, when discussion future changes to the state income tax.