Tax Foundation and Cato Agree: Lower Taxes Make for Stronger States

In the last three weeks, two conservative think tanks — the Cato Institute and the Tax Foundation — have ranked the states based on their tax policies, or lack thereof, and the similarities and differences are striking and instructive. More than that, the lessons learned are being applied by some of the more unlikely governors.

A cursory glance at the top 10 states, according to the Tax Foundation, reveals that eight of them have no state income tax, while each of the bottom 10 levies one. As noted in its Executive Summary:

> Property taxes and unemployment insurance taxes are levied in every state but there are several states that do without one or more of the major taxes: the corporate tax, the individual income tax, or the sales tax.
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> Wyoming (#1), South Dakota (#2), and Nevada (#3) have no corporate or individual income tax. Alaska (#4) has no individual income or state-level sales tax; Florida (#5) has no individual income tax; and Montana (#6) and New Hampshire (#7) have no sales tax.
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> Indiana (#8) and Utah (#9) do levy all three of the major taxes, but do so, according to the Tax Foundation, "with low rates on broad bases" of taxpayers.

This compares to those ranked lowest in its survey:

> The states in the bottom ten suffer from the same afflictions: complex, non-neutral taxes with comparatively high rates. New Jersey (#50), for example, suffers from some of the highest property tax burdens in the country, is one of just two states to levy both an inheritance and an estate tax, and maintains some of the worst structured individual income taxes in the country.

In its report card on America's governors, Cato came up with a different top 10, providing lessons for observers in the process. While the Tax Foundation focused on fiscal policy, rates and structure, Cato took a broader approach:

> Scores ranging from 0 to 100 were calculated for each governor based on seven tax and spending variables. Scores closer to 100 indicate governors who favored smaller government policies.

The governors were then ranked on letter grades "A" to "F." Only four governors scored an "A": Pat McCrory of North Carolina, Sam Brownback of Kansas, Paul LePage of Maine, and Mike Pence of Indiana. Most of those governors earning "B"s were included in the Tax Foundation's ranking of top 10 states.

Both studies were positively ebullient about North Carolina's massive tax reform package passed in 2013, which affected all the state's major taxes. Cato explained:

> Pat McCrory of North Carolina signed into law a major tax reform package in 2013 which replaced three individual income tax rates (6.0, 7.0, and 7.75 percent) with a single rate of 5.8 percent, falling to 5.75 percent in 2015.
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> The package also cut the corporate tax rate, repealed the estate tax, and broadened the sales tax base….
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> Governor McCrory approved further tax cuts in 2014 and he has kept a tight rein on spending.

This resulted in moving North Carolina from #44 in the Tax Foundation's rankings to #16, "the single largest rank jump in the history of the Index," effused the authors at the Tax Foundation, adding,

> The state improved its score in the corporate, individual, and sales tax components of the Index, and as the reform package continues to phase in, the state is projected to continue climbing in the rankings.

The state that differs the most in the rankings is also instructive for lessons learned: New York. In the Tax Foundation's study, New York ranks #49, just above New Jersey and just below California, while New York Governor Andrew Cuomo got a "B" for his work in that state, according to Cato. Said the analysts at Cato:

> Governor Cuomo is one of the highest-scoring Democratic governors in this report. His score is buoyed by a major tax-cut package he signed into law in 2014.
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> The package cut the corporate income tax rate from 7.1 to 6.5 percent, reduced the corporate tax rate on qualifying manufacturers from 5.9 percent to zero, ended a separate bank tax system, ended a surcharge on utility customers, increased the estate tax exemption, reduced the property tax burden on manufacturers, and provided property tax breaks to homeowners.
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> The package was far from perfect, but it showed that Cuomo recognizes that New York's tax climate is uncompetitive and needs improvement.

What it also showed is that Cuomo has been reading the Tax Foundation's dismal rankings of his state for years and has started to apply some of those lessons thus learned. Authors at Cato agreed. Although keeping New York at the bottom of its rankings, they applauded Cuomo for recognizing reality and trying to do something about it:

New York's corporate income tax ranking improved from 24th to 20th as a result of corporate tax reform passed this year, which is starting to phase in. Once fully phased in, the package will lower the corporate rate from 7.1 to 6.5 percent, eliminate the capital stock tax and corporate alternative minimum tax, extend net operating loss carrybacks from 2 to 3 years, and remove the carryback cap.

Once fully phased in, the [state's] corporate tax component of the Index is expected to improve to 4th place.

There are many other components impacting a company's or an individual's decision to move into, or out of, a state besides its tax policies. But for California-based Intel, that state's (#48) oppressive tax policies forced its decision to build a multi-billion dollar chip-making facility employing hundreds of workers in Arizona (#23), instead of California. Northrop-Grumman made the same decision, deciding to move its headquarters from Maryland (#40) to Virginia (#27) in 2010.

The lessons being applied by governors bode well. For years New York has been bleeding companies and citizens seeking warmer and friendlier tax climes. Governor Andrew Cuomo has decided to try to stop the bleeding, as evidenced by favorable comments about his recent tax policies from both Cato and the Tax Foundation. Governor McCrory of North Carolina is already applying the lessons, as well, and the impacts there are already beginning. Right behind McCrory is one of the more unlikely state governors, Democrat Andrew Cuomo of New York.

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