Cautionary Tales From Other States:
Income Tax Cuts Don't Result In Economic Growth

Most researchers who have studied the impact of cutting state income taxes on the state's economic growth find very little correlation – tax cuts do not equal economic growth. Cuts do not pay for themselves by expanding the taxpayer base or increasing economic activity as some have claimed.

Generally, the economies in states that have reduced income taxes have performed more poorly than the national economy overall. Despite this evidence, states continue to make tax cuts and shift taxes from income-based levies to consumption-based levies, leaving less money for states to invest in crucial services and programs like education, infrastructure, criminal justice and health care that help make communities strong and vibrant.

Kansas

In 2012, Kansas lawmakers passed a tax overhaul bill that, along with subsequent changes, sharply reduced the state's income tax rates. Revenues did not increase as projected. In fact, in 2017, five years out, Kansas was facing a structural deficit of close to $1 billion. In June 2017, the Kansas legislature enacted legislation over a gubernatorial veto to roll back most of the income tax cuts for the wealthy. The tax increases are projected to generate $1.2 billion over the next two years to address the structural deficit, and provide additional funding for Kansas' public schools. Prior to this action, over the past 5 years:

- The sales tax rate has been increased two times – once in 2013 and again in 2015 – despite the fact that the 2012 overhaul included a planned *reduction* in the sales tax rate. At a current rate of 6.5%, only eight states have a higher rate than Kansas.
- Early in 2017, the Kansas legislature passed legislation rolling back many of the 2012 income tax cuts, to try to close their budget holes. The Governor vetoed the rollback.
- There have been two successful lawsuits challenging insufficient funding for Kansas' public schools. The most recent decision, issued in March 2017, requires the legislature appropriate hundreds of millions of additional funds by June 30, 2017.
- Kansas' debt has been downgraded three times, and Moody's issued a negative outlook watch after the Governor vetoed the legislature's attempt to raise additional revenues earlier this year.

Ohio

Ohio has been systematically cutting taxes, primarily for businesses, since 2005. A "small business" income tax break passed in 2013 and expanded last year – which exempts the first $250,000 in pass through income and imposes a 3% rate for pass through entities – will cost just under $1 billion in the next two fiscal years, which is $600 million more than estimated at the time of passage. Even though revenue estimates have already been reduced once, Ohio is currently facing a projected shortfall of $400 million in both 2018 and 2019 because the Ohio economy is growing slower than expected, and both the sales tax and income tax are underperforming.

- Ohio's annual average job growth has been 4.7 percent since 2013, compared to the national average of 7.2 percent. Job growth in Ohio has lagged the nation since tax cuts were implemented, with 2016 being the worst year since the end of the recession.
- Even though Ohio has experienced a 19 percent increase in children in agency custody since 2009, primarily due to the statewide drug crisis (Ohio has the highest number of drug overdose deaths in the nation), state funding for child welfare has dropped by $93 million as cuts were made to try to balance the budget.
- Between 2009 and 2016, funding for local government and public libraries has dropped by 39 percent.
- The ratio between income and sales taxes in Ohio has flipped so that now, the sales tax provides the largest share of state revenues. This shift means that as a percentage of income, middle and lower income people have taken on some of what higher income individuals were previously paying.

Louisiana
Louisiana has suffered from revenue shortfalls and budget cuts since 2009, in large part due to a series of tax cuts that began in 2007 when the state was experiencing a boom because oil prices were at an all-time high, and money was flowing in as part of the Katrina/Rita recovery. Because there were extra resources, Louisiana enacted tax cuts that were extended and expanded over the next several years, despite evidence that the Louisiana economy was lagging, and that revenues were substantially less than the amount needed to meet ongoing expenditures. Although slumps in the oil market have played a part in Louisiana's fate, it was primarily the tax cuts that started the sharp decline in revenues and the corresponding structural deficit that Louisiana has so far been unable to recover from. Where Louisiana stands now:

- The state has $4 billion less now that in did in 2007-2008.
- Louisiana has made significant cuts in K-12, higher education, child protective services, juvenile justice, and corrections, including staff reductions of over 30,000 because revenues have been insufficient.
- Last year, to address a shortfall of over $1 billion (relative to the current revenue forecast, not 2007 revenue which is a much bigger gap), the Louisiana legislature enacted a temporary 1% sales tax increase and removed some exemptions from the sales tax. Louisiana currently has the highest combined state/local sales tax rate in the nation at 10%, and despite these increases, revenue shortfalls are predicted for the current fiscal year. Since these measures expire in July of 2018, the legislature is once again facing shortfalls of an estimated $1.5 billion beginning in July 2018.

Oklahoma
Oklahoma started cutting income taxes in 2004, and continued doing so, even in the face of revenue shortfalls and an ever-increasing structural deficit. Beginning in 2004, the top income tax rate in Oklahoma has been incrementally reduced from 6.65% to 5% with a cumulative loss of over $1 billion in revenues that the state would have otherwise had but for the cuts. This has meant that:

- Oklahoma has made more cuts to education funding since the Recession than any other state. State support for K-12 education on a per student basis has decreased 24.2 percent from 2008 to 2016. In April, the state did not have enough funds to issue promised funding to schools, requiring school districts to dip into other operating funds to pay teachers, and move to drastic measures like 4-day school weeks.
- In 2014, the Oklahoma legislature passed a law that automatically reduces the income tax rate when revenue targets are met. More recently, in an effort to balance the budget, the Oklahoma legislature voted to suspend the triggers for this year, and passed several measures that increased taxes to avoid a third consecutive budget shortfall that was estimated to be $878 million in FY 2018 without the recently enacted changes.
- The most recent budget passed by the Oklahoma legislature reduces funding for higher education by 3.8 percent and cuts many other state agencies by 4 percent. Even with these cuts and new revenues mentioned above, Oklahoma is expected to face a deficit in the next fiscal year of over $400 million.

The Bottom Line: These states all reduced taxes or moved from income-based to consumption-based tax systems under the belief that resulting revenue losses would be made up by increased economic activity. The anticipated increases never occurred, forcing deep and painful successive budget cuts and in some cases, new tax increases just to stay even. Despite action by these states during the current year to balance budgets, they all still face significant shortfalls in the future because they have not yet addressed the structural deficits they created by reducing reliance on the income tax. But there is one bright spot - In June, 2017, Kansas ended its "march to zero" by rolling back many of the harmful income tax cuts enacted in 2012 favoring the wealthy that crippled the state and forced painful budget cuts. By taking this action, Kansas can serve as a positive model for other states grappling with these issues.