

Arkansas Tax Policy

Interstate Competition

Presentation to the Arkansas
Legislature
September 20, 2016

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TOPICS OF DISCUSSION

- Overview of Arkansas Tax Policy
- State-Local Tax Burden
- State Business Tax Climate Index

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79 years

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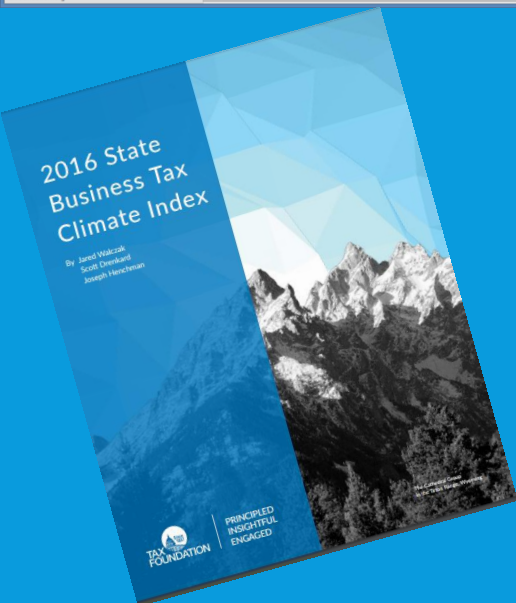
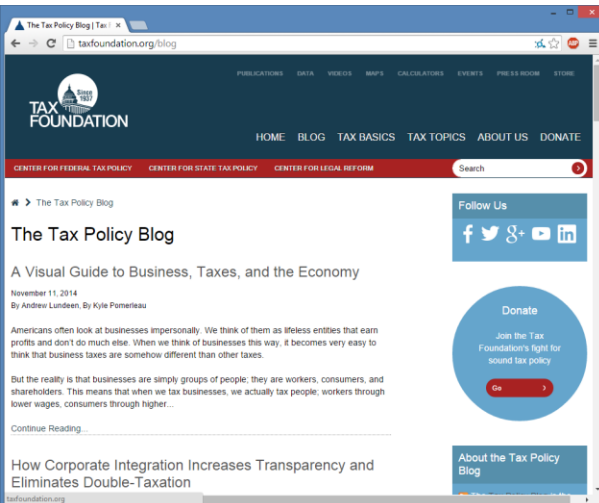
on objective
research,
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& analysis

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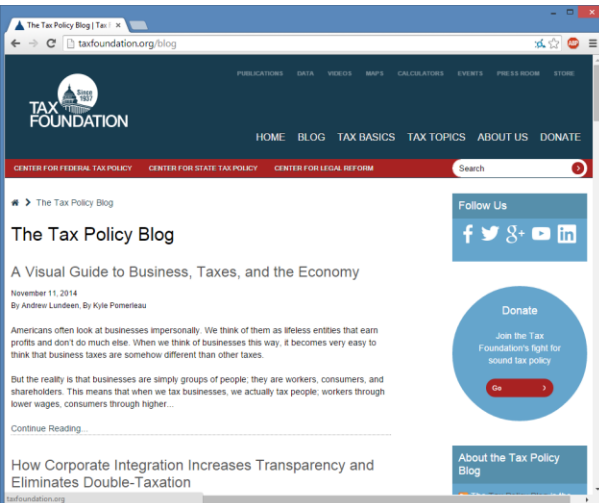
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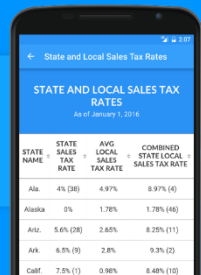
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How do the 2016 Presidential Tax Plans Compare So Far?

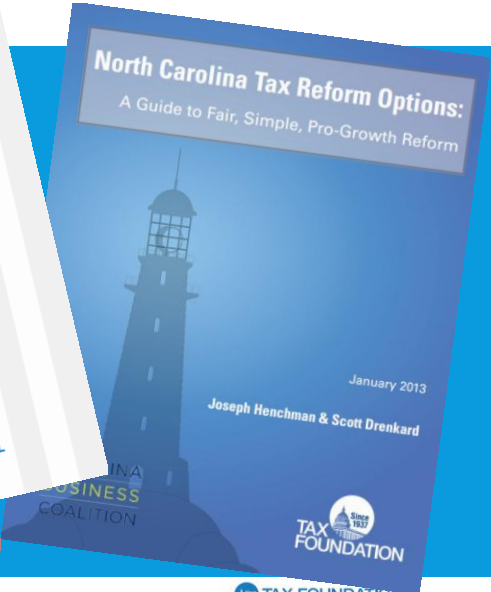
| | Bush | Carson | Cruz | Paul | Rubio | Santorum | Trump |
|---|----------|----------|----------|----------|----------|----------|-----------|
| 10-Year GDP Growth | 10% | 16.0% | 13.9% | 12.9% | 15% | 10.2% | 11.5% |
| 10-Year Capital Investment Growth | 28.8% | 46.6% | 43.9% | 40.5% | 48.9% | 29% | 29% |
| 10-Year Wage Rate Growth | 7.4% | 10.9% | 12.2% | 11.4% | 12.5% | 7.3% | 6.5% |
| Added Jobs (millions) | 2.7 | 5.2 | 4.9 | 4.3 | 2.7 | 3.1 | 5.3 |
| 10-Year Static Revenue Estimate (billions) | -\$3,665 | -\$5,617 | -\$3,666 | -\$1,797 | -\$6,055 | -\$3,223 | -\$11,980 |
| 10-Year Dynamic Revenue Estimate (billions) | -\$1,610 | -\$2,472 | -\$768 | +\$737 | -\$2,401 | -\$1,093 | -\$10,135 |

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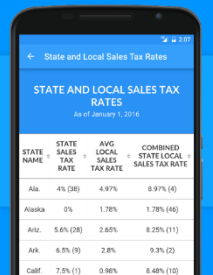


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COMPARATIVE STATE TAX POLICY

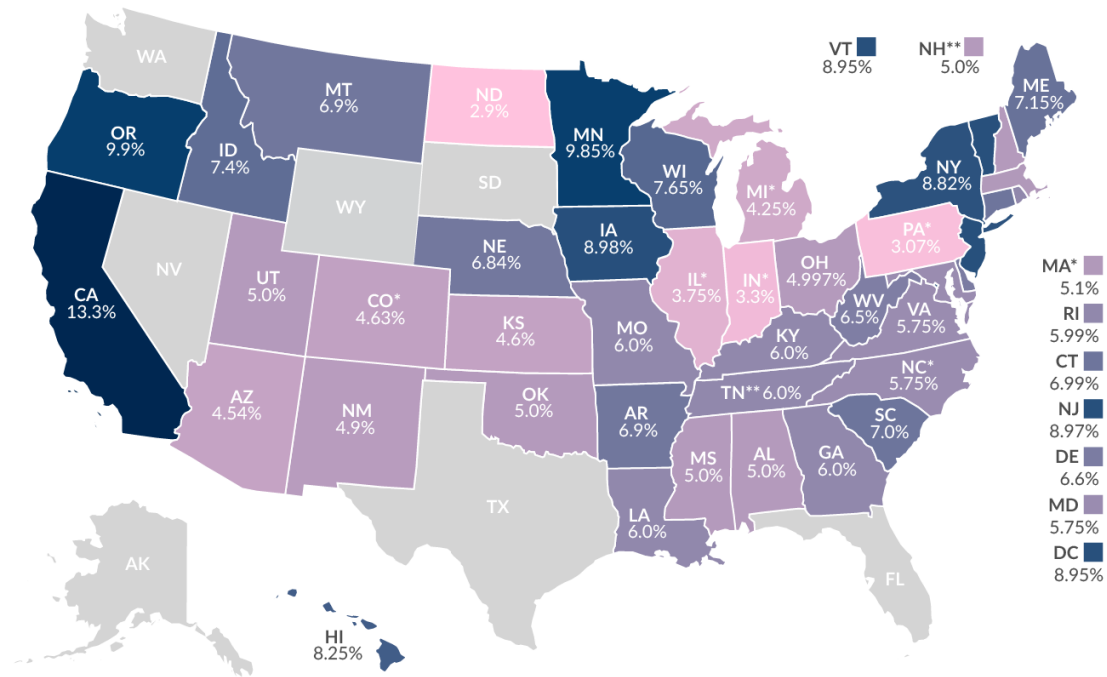
- We think of state tax policy in four large categories.
 - Tax Rates
 - Tax Collections
 - Tax Burdens
 - Tax Structure

TAX RATES

INDIVIDUAL INCOME TAX

How High Are Income Tax Rates in Your State?

Top State Marginal Individual Income Tax Rates, 2016



Note: (*) State has a flat income tax. (**) State also only taxes interest and dividends income. Map shows top marginal rates: the maximum statutory rate in each state. It is not an effective marginal tax rate, which would include the effects of phase-outs of various tax preferences. Local income taxes are not included. Source: State tax forms and instructions.

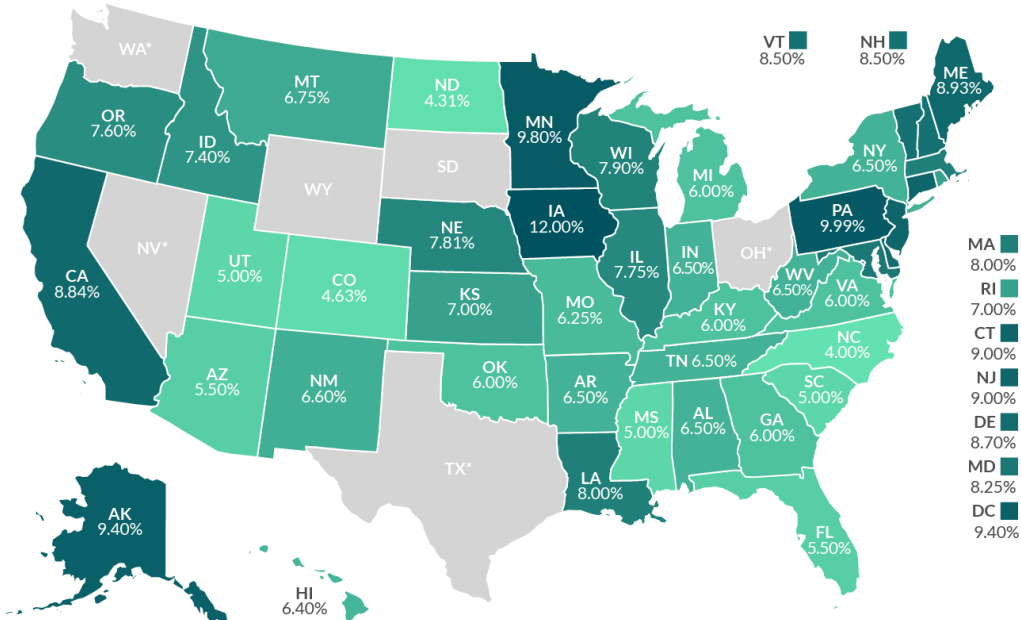


TAX RATES

CORPORATE INCOME TAX

How High Are Corporate Income Tax Rates in Your State?

Top State Marginal Corporate Income Tax Rates in 2016



Note: (*) Nevada, Ohio, Texas, and Washington do not have corporate income taxes but do have gross receipts taxes with rates not strictly comparable to corporate income tax rates. Arkansas assesses a surcharge of 3% of the taxpayer's total liability. Connecticut's rate includes a 20% surtax. Delaware and Virginia have gross receipts taxes in addition to their corporate income taxes. Illinois' rate includes two separate corporate income taxes, one at a 5.25% rate and one at a 2.5% rate. The tax rate in Indiana will decrease to 6.25% on July 1, 2016.

Source: State tax statutes, forms, and instructions; Commerce Clearinghouse.

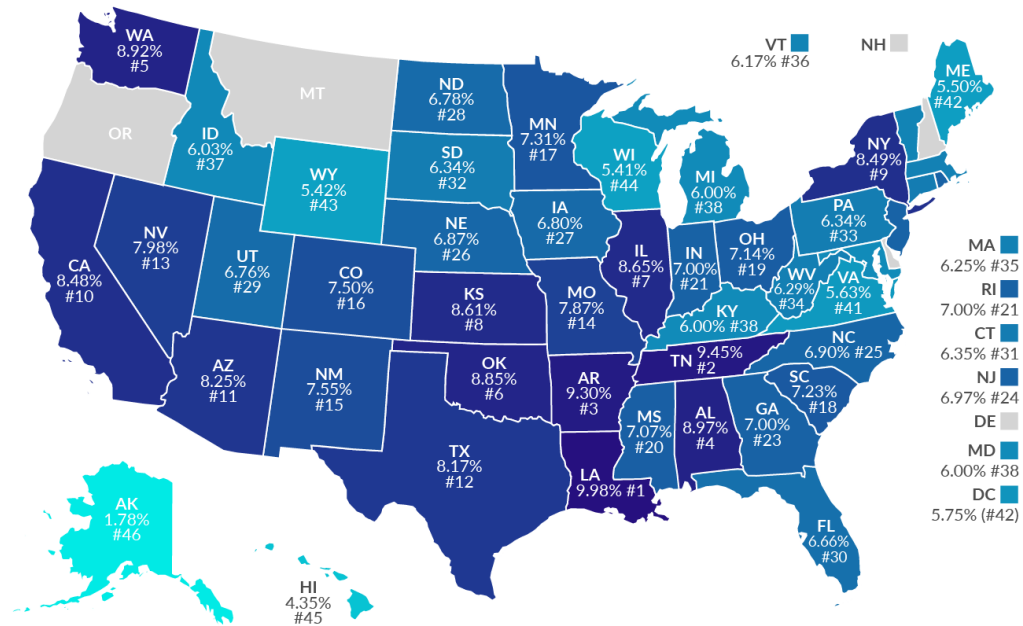


TAX RATES

SALES TAX

How High Are Sales Taxes in Your State?

Combined State & Average Local Sales Tax Rates (July 1, 2016)



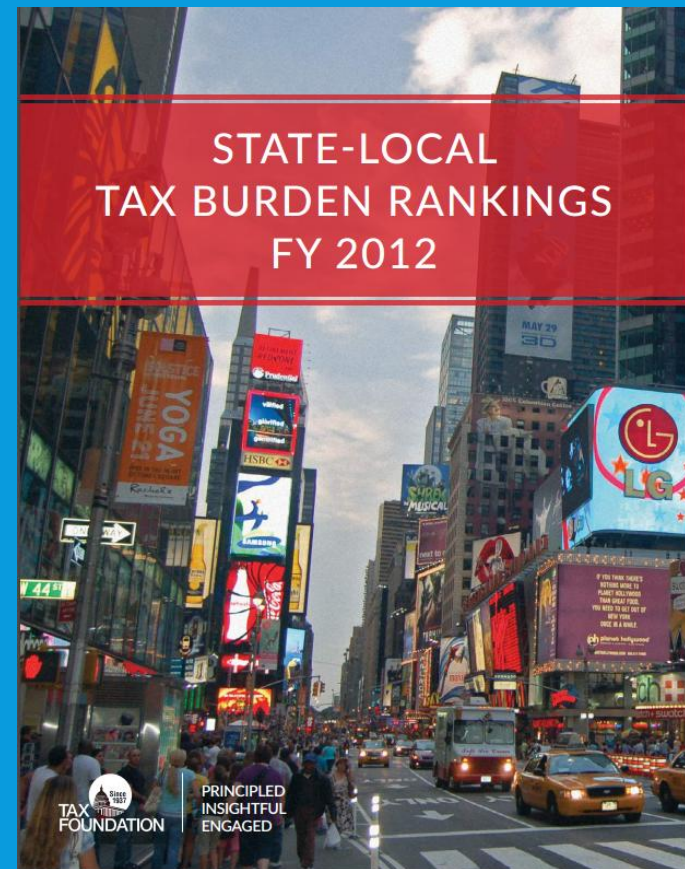
Note: City, county, and municipal rates vary. These rates are weighted by population to compute an average local tax rate. Three states levy mandatory, statewide local add-on sales taxes at the state level: California (1%), Utah (1.25%), and Virginia (1%). We include these in their state sales tax rates. The sales taxes in Hawaii, New Mexico, and South Dakota have broad bases that include many business-to-business services. Due to data limitations, the table does not include sales taxes in local resort areas in Montana. Some counties in New Jersey are not subject to statewide sales tax rates and collect a local rate of 3.5%. Their average local score is represented as a negative.

Source: Sales Tax Clearinghouse, Tax Foundation calculations, State Revenue Department Websites



STATE-LOCAL TAX BURDEN

- Tax burden is the portion of income that goes to taxes
- Tax collections is amount received by state; tax burden is amount paid by residents
- Incidence: Gasoline taxes
- Incidence: Corporate income tax



STATE-LOCAL TAX BURDEN

TAX INCIDENCE

Legal Incidence is Different from Economic Incidence

Example: Gas Taxes



State government dictates that service station businesses must collect taxes on the purchase of gasoline.

Service stations bear the legal incidence of the tax.



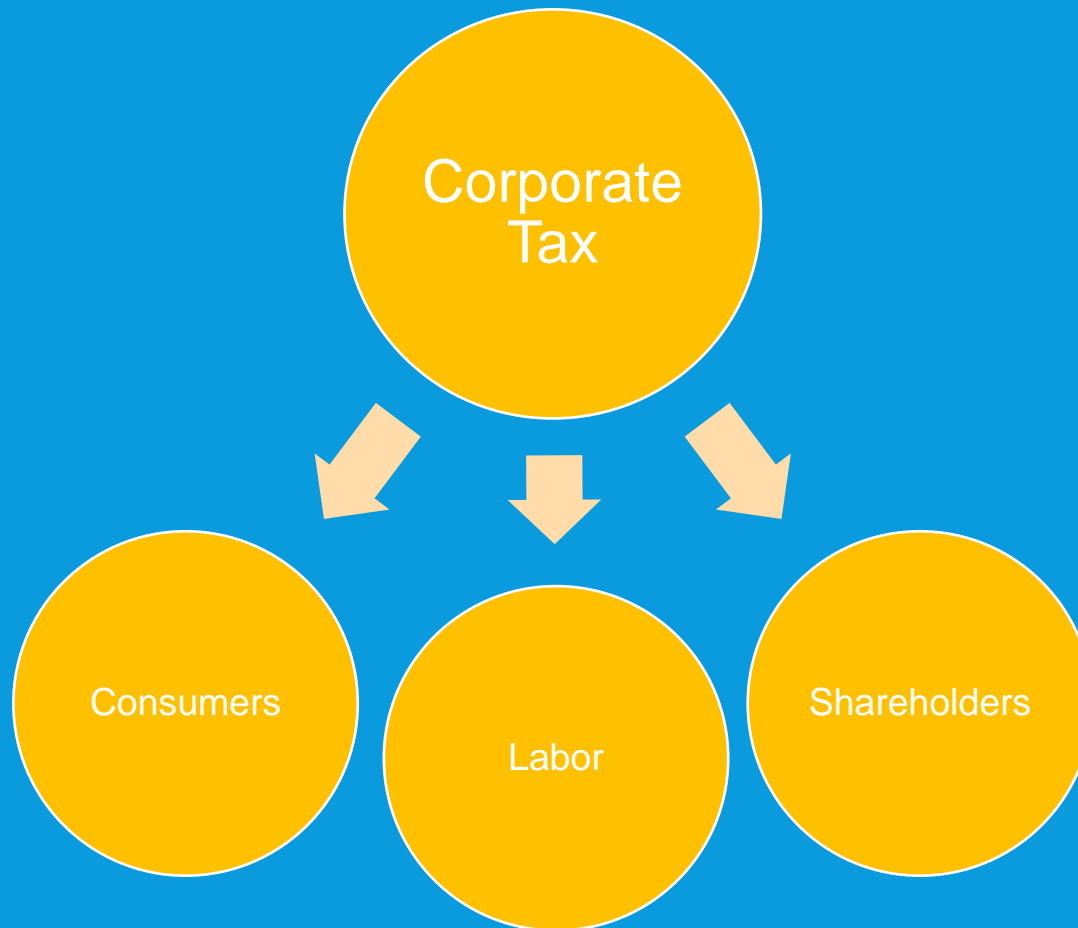
Customers buy at service stations, which have shifted the tax forward to customers by increasing the price.

Customers bear the economic incidence of the tax.

Businesses send tax collections to the state government. Even though the business has physically sent the money to the government, it did not bear the economic burden of the tax.

STATE-LOCAL TAX BURDEN

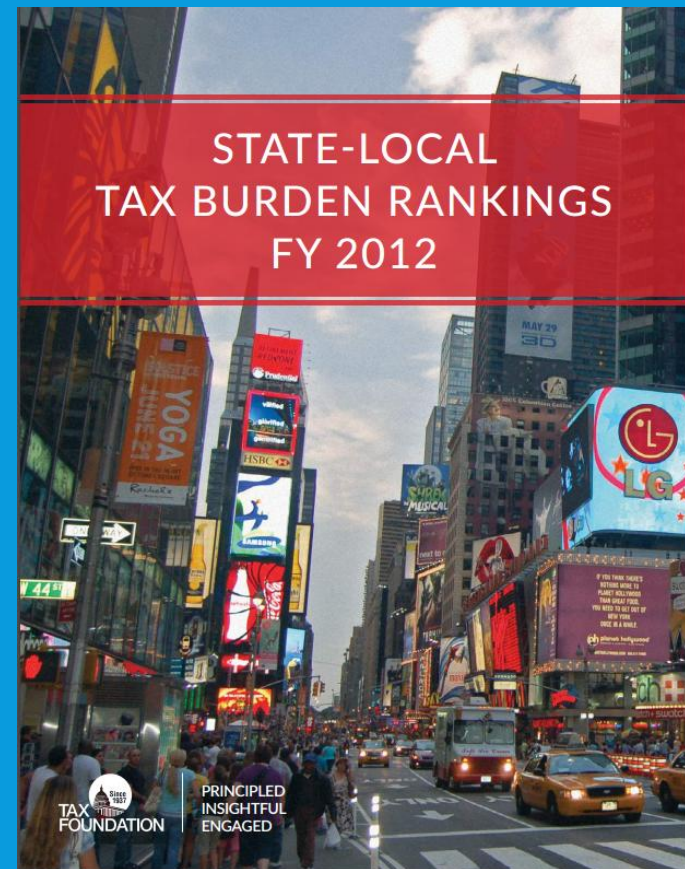
TAX INCIDENCE



STATE-LOCAL TAX BURDEN

ARKANSAS, FY 2012

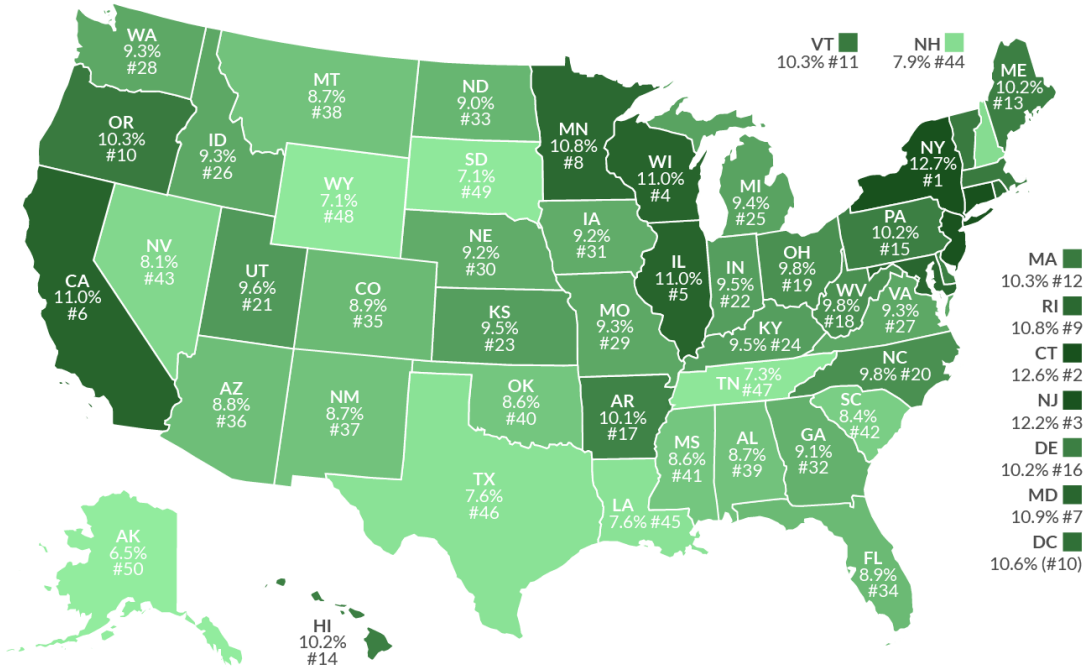
- 10.1 percent
- 17th highest
- \$2,552.18 to in-state governments and \$966.83 to out-of-state governments



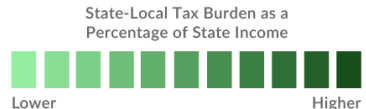
STATE-LOCAL TAX BURDENS

State-Local Tax Burdens by State

State-Local Tax Burdens as a Percentage of State Income, FY 2012



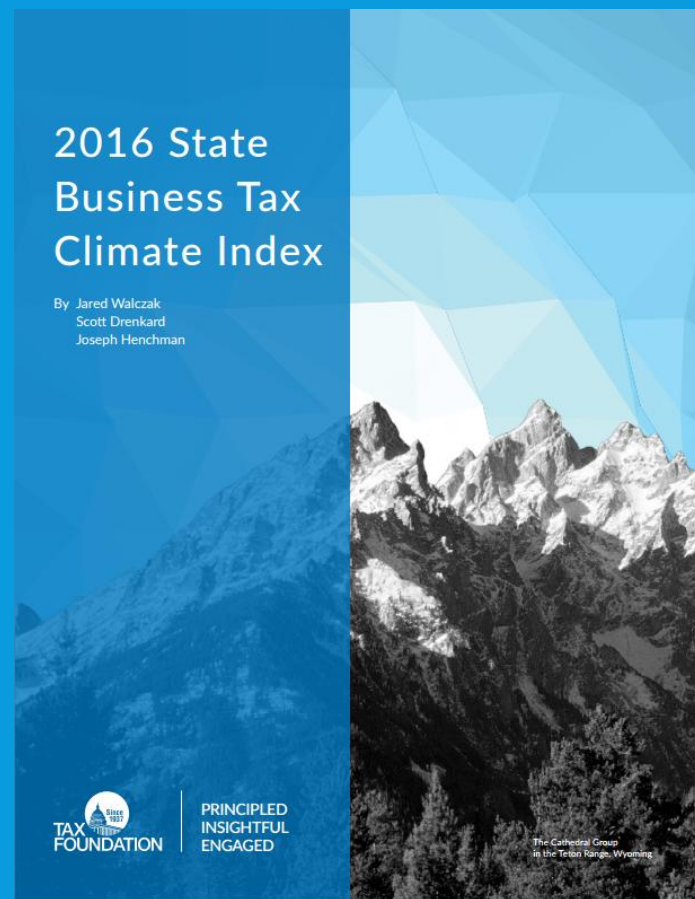
Note: As a unique state-local entity, Washington, DC is not included in rankings, but the figure in parentheses shows where it would rank.
 Source: Tax Foundation calculations, U.S. Census Bureau, Rockefeller Institute, Bureau of Economic Analysis, Council on State Taxation, and Travel Industry Association.



STATE BUSINESS TAX CLIMATE INDEX

MAJOR STUDIES

- Comprehensive look at state tax structures
- The **how** rather than the **how much**
- Five areas of tax:
 - Individual income taxes
 - Corporate income taxes
 - Sales and excise taxes
 - Property taxes
 - Unemployment insurance taxes



STATE BUSINESS TAX CLIMATE INDEX

Overall: 38th

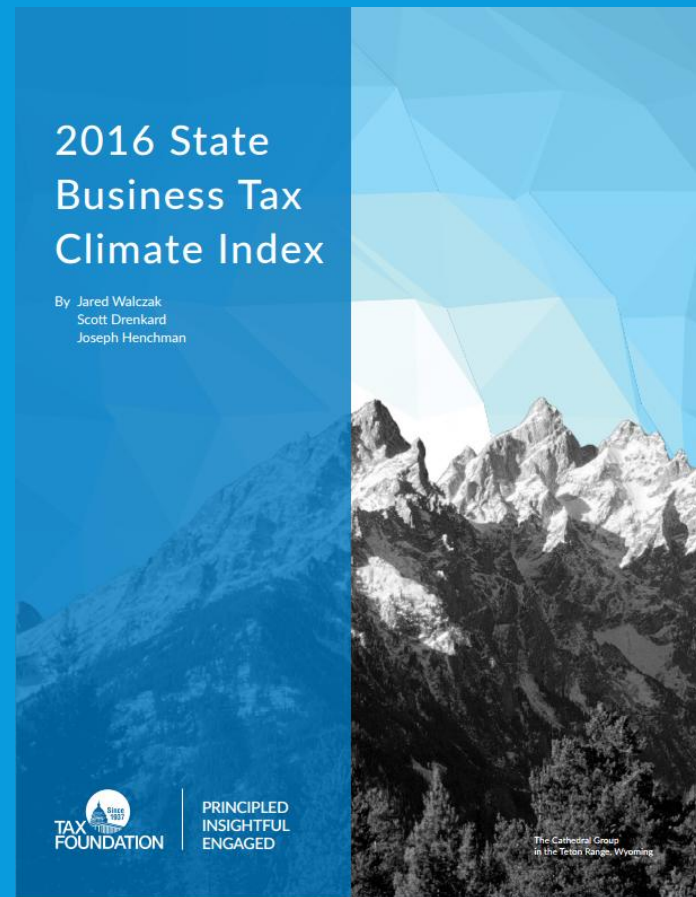
Corporate: 42nd

Individual: 29th

Sales: 43rd

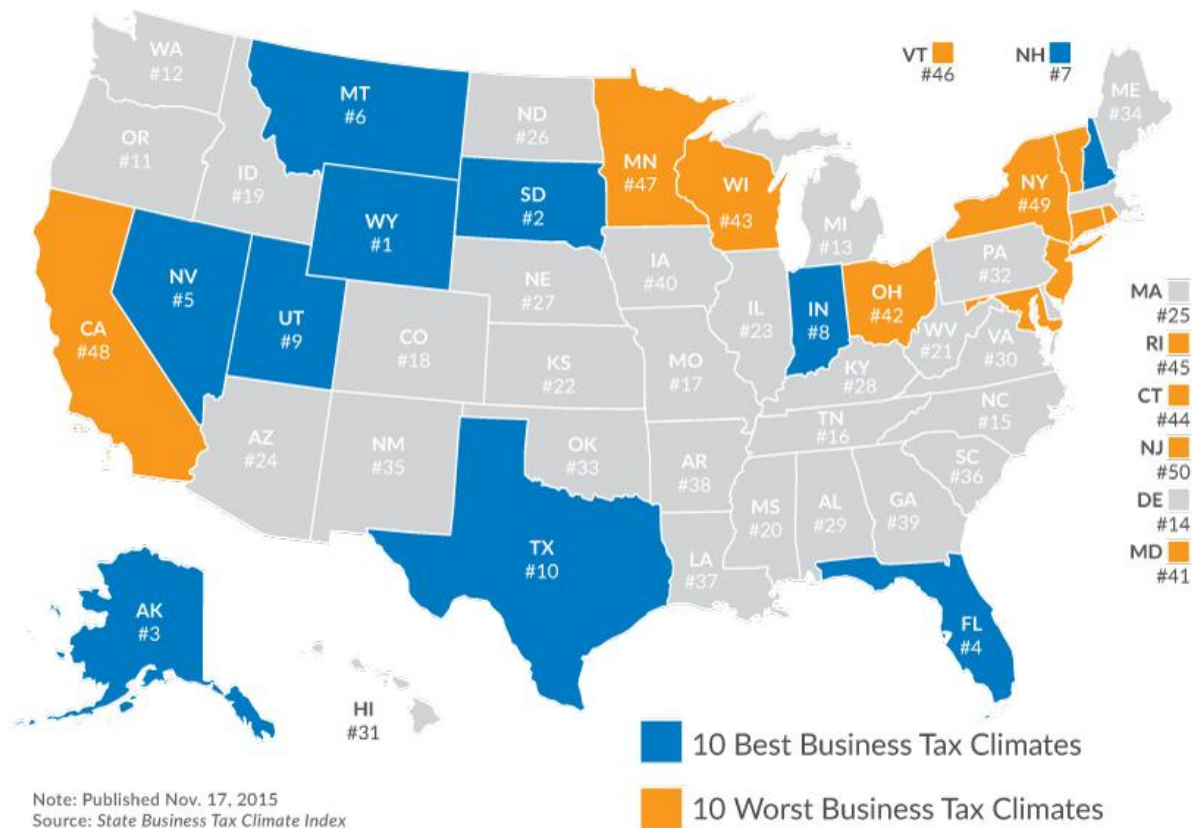
Unemployment Insurance: 43rd

Property: 27th



STATE BUSINESS TAX CLIMATE INDEX

2016 State Business Tax Climate Index



STATE BUSINESS TAX CLIMATE INDEX

CORPORATE INCOME TAX

- Arkansas's rate is 24th highest and higher than many neighboring states, and it has more brackets.
- NOLs lag other states at 0/5 years.
- Arkansas still uses a throwback rule.
- Arkansas has a number of distortionary credits.

2016 State Business Tax Climate Index

By Jared Walczak
Scott Drenkard
Joseph Henchman



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STATE BUSINESS TAX CLIMATE INDEX

CORPORATE INCOME TAX

- Arkansas's 6.9 percent top rate is 14th highest and higher than many neighbors.
- Three rate schedules with four to six brackets each creates complexity.
- Arkansas has a marriage penalty.

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SALES TAX

- Arkansas's combined state-local sales tax rate (9.3 percent) is the third highest in the country, behind only Tennessee and Louisiana.
- Arkansas includes a number of business inputs in the sales tax base, such as machinery and equipment and some business services.

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PROPERTY TAX

- Arkansas still has a franchise tax, one of only 17 states with such a tax.
- Arkansas also taxes inventory, one of only 14 states to include it in the property tax base.

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CONCLUDING THOUGHTS

- A package of reforms can tremendously help Arkansas's competitiveness.
- Cutting revenue does not have to be the only criterion. Many of these reforms can be combined to offset revenue losses.
- Tax triggers can mitigate concerns about revenue availability.

QUESTIONS AND FEEDBACK

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