EXHIBIT C

Briefing Memo on Arkansas Tax Policy:

Prepared for the Arkansas Tax Relief and Reform Taskforce
By Arkansas Advocates for Children and Families
MAY 5, 2017

PURPOSE: To provide context and summarize tax reform recommendations that prioritize Arkansas children and families.

CURRENT SITUATION: Although our economy is recovering, our state budget is not keeping up. A revenue shortfall has caused a $70 million cut to the 2017 fiscal budget and a recent $43 million budget cut for fiscal year 2018. This results from previous decisions to cut personal income taxes. Tax cuts made during the 2013 and 2015 sessions cost $242 million in general revenue in 2017. Most recently, Governor Hutchinson signed Act 79, a $50 million tax cut for those making less than $21,000 a year in taxable income.

In Arkansas, the portion of a family's paycheck that goes to state and local taxes taxes is twice as high if you earn a middle-income or lower wage compared to those in the top one percent. Our state and local tax system asks middle-income families (with incomes ranging from $28,000-$47,000 a year) to pay 11.4 cents in state and local taxes for every dollar they earn. In contrast, the top one percent of earners (who make over about $350,000 a year) pays less than six cents on the dollar.

RECOMMENDATIONS: Our recommendations protect the budget and focus on long-term business- and family-friendly strategies.

- **FOR GROWTH, FOCUS ON PUBLIC INVESTMENTS**. State economies are stronger and more competitive when we have good schools; a well-educated and well-trained workforce; good highways and roads; safe communities with responsive police and fire protection; community amenities like parks and the arts that attract workers; and when businesses have access to markets. Our economy is also stronger when all Arkansans have the resources and opportunities they need to be productive workers. This requires public investment. Taxes, however, don't matter very much for economic growth. State-level differences in taxes or tax cuts do not drive business location decisions nor are they major drivers of economic growth. There is little correlation between state personal income tax rates and state growth in employment, investment, productivity, or per-capita GDP. High-income earners are typically the biggest winners from big cuts in personal income taxes. The biggest losers are inevitably families who work low-paying jobs, and the services those families rely on.
- **BOOST LOCAL ECONOMIES WITH TAX CREDITS FOR WORKING FAMILIES**. An Arkansas Earned Income Tax Credit (EITC) would supplement the federal version which is responsible for lifting 6.2 million people out of poverty every year, including 3.2 million children. EITCs have strong support from members of the

business community who know that customers with access to tax credits are better able to stay up-to-date on their bills and more likely to spend money at local businesses. A state EITC pegged at five percent of the federal credit would put about $40 million annually into the pockets of Arkansans who work hard and are paid so little they struggle to make ends meet.

- **Close loopholes and unnecessary exemptions**. Eliminating capital gains tax cuts that primarily benefit the very wealthy, placing sensible limits on itemized deductions, and closing corporate loopholes would secure our fiscal future and reduce the disparities in tax burdens between income groups. Itemized deductions currently cost the state about $258 million a year, and only a tiny fraction of these benefits goes to middle- and low-income working families. We can also level the playing field for local businesses by requiring all corporations to file a combined report. That would close the loophole that allows corporations who operate in multiple states to pay much less than the mom-and-pop stores who only operate in Arkansas.
- **Modernize our sales tax**. If we clean up our sales tax structure in a smart way, we could make taxes fair for all and have funds to invest in summer reading classes, quality pre-K, and other programs for our kids. Arkansas state revenue is being nickeled and dimed by special-interest tax breaks. Many things that working families purchase are taxed; many things valued by large corporations are not. Just eliminating the tax break on rental cars, charter planes, and newspaper sales and advertisements would save Arkansas $24.1 million a year. Other states are also lining up for huge revenue gains by taxing digital goods, collecting taxes due on internet sales, and by closing the online hotel tax loophole that allows travel companies like Priceline to skirt parts of the sales tax code.
- **Update highway funding strategies**. Arkansas has a structural highway funding problem. We need good roads and other infrastructure to keep our economy healthy. But we must pay for that in a way that doesn't overburden low-income families or leave the programs they rely on underfunded. The solution for the highway funding dilemma is a modernized fuel tax. We should increase our fuel tax to meet funding needs today, but also make sure the entire fuel tax is indexed appropriately so that highway needs are met in the future. Gas tax revenue, the biggest state revenue source for highways, has been eaten away by inflation and more fuel-efficient cars. The costs of asphalt, labor, and all road maintenance have gone up, but our fuel tax hasn't increased since 2001. Also, because cars become more fuel-efficient every year, Arkansans are buying less gas and contributing less per mile to road maintenance. The fuel tax index should be tied to both inflation and fuel efficiency so that highway funding grows with the cost of keeping safe, up-to-date roads. Because gas taxes are harder on working families, any increase to fuel tax should be paired with a measure to help working families keep more of what they earn, like a state Earned Income Tax Credit (EITC).

For more information, contact:

Eleanor Wheeler, Senior Policy Analyst**,** ewheeler@aradvocates.org

Tamika S. Edwards, J.D., Director of Governmental Affairs**,** tedwards@aradvocates.org

Rich Huddleston, Executive Director**,** Rhuddleston@aradvocates.org