



Chairman Oelslager, Vice-Chair Coley, Ranking Member Skindell, and members of the committee, my name is Joe Testa, and I am Tax Commissioner of the Ohio Department of Taxation (ODT). Thank you for the opportunity to testify today on two important matters: the budget request for ODT, and the tax reform proposals contained in Governor John Kasich's Fiscal Years (FY) 2016-2017 budget.

May I first offer a sort of preface to my testimony? It's brief; consists of only one word. That word is 'jobs'. Jobs and the need to create jobs underlie all aspects of the tax proposals I'll be discussing during the course of my testimony. As you know the governor has that one word foremost in his mind every day.

I'd like to start by briefly providing some context in which to consider the two budget related issues I'm testifying on here today. We have to look back in time to fully understand how we arrived at the proposals we'll be discussing. As well, we have to look forward to what we want from our state government and how that will mesh with and contribute to where we want Ohio to be in the future.

Working together, the Governor and the General Assembly provided \$3 billion in tax reductions for Ohioans. Cuts included eliminating the estate tax, reducing the state income tax rate by 10 percent, creating a 50 percent income tax deduction for small business owners (temporarily increased to 75 percent for 2014) and giving targeted tax relief to low- and middle-income workers. Today, Ohio is

continuing to progress with 340,000 new private sector jobs since 2011 and an unemployment rate of 5.1 percent – down from 9.2% at the beginning of 2011. Ohio incomes are growing faster than the national average and Ohio exports topped \$52 billion in 2014 – a state record, placing it 9<sup>th</sup> within the United States. According to the Ohio Secretary of State, total new business filings have reached record highs in each of the past four years. In the 8<sup>th</sup> edition of *Rich States, Poor States*, Ohio’s economic outlook has improved from 42<sup>nd</sup> in 2010 to 23<sup>rd</sup> in 2014. Governor Kasich wants to continue this growth by delivering a net tax cut of \$523 million in this upcoming two-year budget.

Before we get to the specific details on tax reform, I’d like to share with you an overview of ODT’s proposed budget.

### **ODT BUDGET AND OPERATIONS**

ODT administers and enforces 30 different state and local taxes and fees, including the state and school district individual income taxes, state and local sales taxes, and an array of business and excise taxes, plus it supervises Ohio’s 88 county auditors in the administration of local property taxes. ODT is headquartered in Columbus, and has more than 200 telecommuters located throughout the state. Collections from taxes and fees in Fiscal Year 2014 generated more than \$26 billion to support many functions of state and local government.

### **OPERATIONAL CHANGES: CUTTING COSTS, INCREASING EFFICIENCY**

During FY 2014-2015, ODT developed and implemented the following operational changes:

- Enhanced measures to protect the state treasury and taxpayer dollars from income tax fraud related to identity theft.
- Reduced staff by 22 percent, or 302 full time equivalent positions since 2011. Our FY 16-17 budget request is for a staff size of 1,075.
- Conducted a comprehensive review of forms used both internally by employees and externally by taxpayers and eliminated more than 130.
- Transferred wireless 9-1-1 fee administration from the Public Utilities Commission of Ohio to ODT, with the addition of pre-paid cell phones.
- For employer withholding taxes, made electronic filing mandatory and established bulk file upload through the Ohio Business Gateway (OBG) for third-party payroll processors.
- For the commercial activity tax (CAT), mandated electronic filing for annual filers and instituted an automated refund claim process to notify taxpayers of overpayments stemming from amended returns.
- Created a portal for county auditors to use to verify the income of homestead exemption applicants. Since the portal began February 2014, 74 counties have made approximately 5,000 income verification inquiries.
- Ohio became a full member of the Streamlined Sales Tax Project. It had been an associate member since the project began.
- Began emailing notices to taxpayers who filed an incomplete personal and/or school district income tax return asking them to complete the process. The program reduced billing notices and mailing costs.
- Consolidated our leased footage from nearly five full floors down to two at the State Office Tower.

## **AGENCY PRIORITIES FOR FY 2016-2017**

- Leverage technology to increase operational efficiencies, improve customer service, and modernize the tax system.
- Strengthen ODT through proven human resources initiatives including more comprehensive evaluations and a merit-based program rewarding high performing employees with more flexible working hours.

## **BUDGET REQUEST FOR FY 2016-2017**

Since FY 2010, ODT has consistently reduced General Revenue Fund (GRF) operating expenses even as revenue collections have increased. ODT's actual general operating expenses for FY 2014 were 22.5 percent less than FY 2010 (*see Attachment A*).

ODT's all funds budget request for FY 2016-2017 is a 10.8 percent decrease from FY 2015.

Through sound fiscal planning and a focus on these initiatives, ODT is able to achieve its primary objectives and reinforce the governor's efforts to continue growing Ohio's economy, stimulating job creation, and providing even greater relief for all Ohio taxpayers.

Over and above the general operating budget, ODT is submitting an Activity B budget request for \$6,865,033 a year for FY 2016 and FY 2017. This funding is essential in ODT's efforts to protect the state treasury from being raided by criminals with stolen ID's filing fraudulent individual income tax refund requests. ODT is currently partnering in such a contract with the Ohio Department of Public Safety for Calendar Year 2015. We hope to continue this partnership through FY

2016-2017, and perhaps expand it to include other state agencies that may have been or potentially will be victimized by criminals utilizing personal information obtained through identity theft.

### **STATE TAXATION ACCOUNTING AND REVENUE SYSTEM (STARS)**

The State Taxation Accounting and Revenue System (STARS) project, financed primarily using Certificates of Participation (COPs) funds, continues to progress through the development phase with Hewlett-Packard (HP) as the contractor. The objective of the STARS project is to consolidate 27 different systems into one integrated system that is developed in a modern architecture to meet industry standards and reduce risk. STARS is expected to provide ODT the flexibility to respond to changes in tax administration and processing, as well as lower the cost of maintenance by consolidating platforms and programming languages. This is a highly complex project that will provide significant improvements in how ODT will conduct tax administration in the future.

Development had been very slow in the early years, prompting a project reset in July of 2012. As part of that reset, the STARS project adopted the Agile development methodology which has facilitated significant progress. The first STARS release occurred in October of 2013 and to date the STARS team has successfully implemented four releases with a total of eight tax types now in production including the employer withholding and sales and use taxes. Release 5, which includes four additional tax types, is near the end of the testing phase with a planned release date of June 1, 2015. By the end of calendar year 2015, we plan to have at least one more release in production.

## **COMBATING TAX FRAUD**

The filing season for Tax Year 2014 has now come to a close for non-extension filers. We are still busy dealing with an unfortunate trend that escalated last year. As you are aware, ODT was flooded with fraudulent refund requests. In recent years, ODT would typically intercept and block fewer than 10,000 fraudulent returns requesting \$8 to \$10 million in tax refunds. Last year, ODT intercepted more than 65,000 income tax returns that, in total, were seeking to steal refunds totaling more than \$278 million.

In order to better protect Ohio taxpayers and prevent tax fraud, ODT implemented additional safeguards that – unfortunately, and unavoidably – caused many refunds to be delayed this filing season. To further bolster the systems that detect and counter refund fraud related to identity theft, an additional up-front filter was applied to all tax refund requests to analyze the demographic information reported on a return and then determine how the return will be further processed by ODT. As we received data and feedback throughout the filing season, tweaks were made to the identity authentication process in order to reduce refund delays to legitimate taxpayers while ensuring the security of taxpayers’ refunds.

When a return is tagged for review, ODT’s additional security measures require those taxpayers to successfully complete an Identity Confirmation Quiz before the return will continue to be processed. If a taxpayer’s return is selected for identity confirmation, the taxpayer receives a letter from ODT directing them to our website ([www.tax.ohio.gov](http://www.tax.ohio.gov)). The website provides access to the quiz, detailed instructions on how to complete it including a video, and frequently asked

questions for reference. Taxpayers without Internet access can call ODT for direct assistance from our taxpayer representatives.

This additional screening and security unfortunately slows the processing of electronic and paper returns, and the issuance of refunds. Electronic returns requesting a refund may take up to 15 days to be direct deposited this year, and paper returns could take up to 30 days for a physical check to be mailed out.

We don't like it; we have always prided ourselves on getting refunds issued quickly. That said, ODT is committed to aggressively fighting tax fraud and protecting taxpayers and their tax dollars.

At this time we don't have a complete picture of attempted tax fraud for this filing season but do have some indications that activity levels were up over last year. We have sent out more than 1.5 million letters to taxpayers and about 100,000 of those individuals have not taken the quiz or verified their identity in sixty days or more. We suspect a significant percentage of those non-responses to be attempted theft.

In the next few months, we will evaluate options available to keep Ohio's taxpayers protected for the next tax season.

Shifting topics now . . .

## **TAX REFORM AND TAX CHANGES**

### **THE CONTINUING NEED FOR TAX REFORM**

Tax reform continues to be one of the most controversial subjects in states across America. But, that is no reason to shy away from it as it plays such an important

role in better aligning our tax structure to reflect our changing economy and propel further growth.

The governor's first stated objective is to encourage investment, risk taking, and job creation. This tax proposal, which provides long-overdue reforms in several areas of Ohio's tax code, eliminates income taxes for virtually all small business owners and investors and lowers the state income tax rate. The proposal will make Ohio more attractive to entrepreneurs, investors, and companies looking to start or relocate a business in a supportive, lower-cost environment. The ultimate goal is job creation. Revising Ohio's tax system, together with budget capacity from the efficient management of state government, will not only bring needed income tax relief, it will help create more employment opportunities for Ohioans.

Our hometown businesses are an essential part of the fabric of our communities and we need to keep it that way. Think for a minute what our communities would look like without those small, local businesses that are such an important part of the fabric of our hometowns.

The governor's second objective in this FY 2016-2017 budget proposal is to continue the movement of Ohio's tax system away from its historical reliance on taxing income to a more contemporary alignment with taxing consumption. Raising the sales tax rate and slightly expanding the base of services subject to sales tax will help enable another significant cut in income tax that tallied up will leave more money in the pockets of all Ohio income taxpayers. In addition to letting people keep more of their own money, this movement from taxing income to taxing consumption provides other benefits. It will better align the state's tax system with the increasingly robust service sector in our economy.

I'd like to first give you the Cliff Notes summary of the governor's proposed tax package. There are a lot of elements involved, and I will provide more detail on each, but I think it will be helpful for you to hear the entirety of the tax changes involved. As I mentioned, collectively, this proposal will deliver a \$523 million net tax cut including state and local changes over the FY 2016-2017 period. Here's how:

***Eliminate Tax on Business Income for Virtually All Ohio Small Businesses:***

Owners of and investors in small businesses with annual gross receipts of \$2 million or less as reported on their federal tax return would pay no tax on the income from their business. This will impact about 98 percent of the approximately one million Ohio businesses structured as sole proprietorships or pass-through entities such as partnerships, S-corps, and limited liability companies.

***Cut Income Taxes for All Ohio Income Tax Payers by 23 Percent:*** The tax cut would start with an immediate reduction of 15 percent in the first year (retroactive to January 1, 2015), and an additional reduction of 8 percent in the second year, reducing Ohio's top rate from 5.333 percent in 2014 to 4.106 percent in 2016. This would move Ohio from the 23<sup>rd</sup> lowest income tax rate in the nation, all the way up to 12<sup>th</sup> (*2015 State Income Tax Rates, Federation of Tax Administrators*).

***Increase Personal Exemptions for Low- and Middle-Income Ohioans Beginning in 2015:*** For Ohioans earning less than \$40,000 a year, the personal exemption would increase from \$2,200 to \$4,000, and for those earning between \$40,000 and \$80,000 a year, the exemption would increase from \$1,950 to \$2,850.

***Increase Tobacco Taxes:*** Ohio's cigarette tax would increase from \$1.25 to \$2.25 per pack; other tobacco product taxes, including a new Vapor Products Tax, would rise to a tax level equivalent to that on cigarettes.

***Raise the Sales Tax Rate and Broaden the Sales Tax Base:*** The budget proposes to raise the sales tax from 5.75 percent to 6.25 percent and expand the sales tax base to include a few more services. The sales tax changes also include a proposal to reduce the tax credit for the value of a used car or boat traded-in on the purchase of a new car or boat, and to place a monthly cap on vendor discounts.

***Modernize Ohio's Severance Tax on Natural Gas and Oil:*** The governor proposes new fixed rates for oil, natural gas and natural gas liquids (6.5 percent at the wellhead, 4.5 percent downstream), no tax on small producers, fully funding state regulatory operations, and dedicating 20 percent of the remaining severance tax revenue for local communities to help them deal with the impact from horizontal drilling activity, both now and in the future. These tax rates would put Ohio in the competitive mid-range of rates charged by other natural gas and oil producing states.

***Adjust the Commercial Activity Tax Rate:*** The proposal would change the CAT tax rate for the first time since it was enacted, from 0.26 percent to 0.32 percent, while also reducing the minimum tax owed by businesses with gross receipts between \$1 million and \$2 million from \$800 a year to \$150.

***Enact a \$100,000 Means-Test on Some Income Tax Credits and Deductions:*** This proposal would change the availability of five Ohio income tax credits and deductions by limiting them to households with incomes less than \$100,000 a year. Those with higher incomes could no longer take these tax credits and deductions.

I'd like to talk now in more detail about the Governor's tax reform proposals.

## **INCOME TAX CUTS**

The tax cuts all target Ohio's income tax and will benefit nearly all small business owners and all Ohio taxpayers, with an additional focus on low- and middle-income taxpayers.

**No Income Tax for Small Businesses:** There are more than one million businesses in Ohio organized as sole proprietorships, or pass-through entities (PTEs) such as partnerships, subchapter S corporations or limited liability corporations (*see Attachment B*). As part of the FY 2014-2015 budget, the concept of the small business investor income deduction (SBD) was introduced and signed into law, benefiting those taxpayers who report PTE business income on their own individual tax returns. In Tax Year 2013, almost 400,000 tax filers took advantage of the SBD, resulting in approximately \$350 million of tax savings.

As part of the FY 2016-2017 budget, Governor Kasich is proposing a new "gross receipts" test that will eliminate income tax for more than 98 percent of those businesses structured as PTEs. If the business has annual gross receipts of \$2 million or less as reported on their federal tax return, then the business owner or investor would not pay Ohio income tax on the related net business income. This dramatic tax cut will free up an additional \$350 million a year in capital that Ohio business owners can use in ways they determine is best for their company. Their decisions will collectively result in new investments that benefit their operation and their customers.

According to the Small Business Administration, small businesses employ more than 47 percent of the private sector workforce. This tax cut is an effort to support and help grow those businesses. By itself, the deduction may not be sufficient to fully pay for and hire a new employee but it could mean that a small business is able to purchase advertising, or equipment, or offer its existing employees more hours to help grow the business. It may also provide the extra capital needed that, when combined with other income or with the tax savings of the other business owners, allows the business to hire an employee. And just as important, it may help a business operating on the margin to meet payroll or to keep its doors open. Every dollar counts to the small business owner.

Together these smaller businesses generate about 43 percent – more than \$11 billion – of all the income earned by companies structured as PTEs. Let them keep more of their own resources to work with and some will become larger businesses. Speaking of which, for those businesses larger than \$2 million, the governor's budget would maintain Ohio's 50 percent tax deduction on the owner's first \$250,000 of net business income.

***Cut Income Taxes for All Ohio Income Tax Payers by 23 Percent:*** Personal income tax rates would be cut for all Ohio income taxpayers by 23 percent over two years, with an immediate reduction of 15 percent. The governor's proposal reflects his agreement with economists who believe income taxes negatively impact economic growth, impede job creation and contribute to the migration of people to low-tax states (*see Attachment C*). This phenomenon has resulted in more than \$12 billion in income leaving Ohio from 1995 to 2010 for states with lower income taxes (*How Money Walks, Travis H. Brown, 2013*). The tax cut will be

phased in, starting with an immediate reduction of 15 percent in year one, and an additional 8 percent in year two. This change means Ohio’s top marginal rate will have been cut from 5.925 percent in 2011 to 5.333 percent in 2014, and then further to 4.106 percent in 2016. Withholding rates will also be adjusted in both years to reflect the reductions. The first change is scheduled for September 2015. This means that the first cut of 15 percent would already be in effect back to January, if the legislature approves the cut.

**Additional Tax Relief for Low- and Middle-Income Ohioans:** During the previous four years, Governor Kasich and this legislature enacted and then doubled an earned income tax credit. That alone provides about \$60 million of tax relief a year to lower income households. In 2013, the personal exemption was \$1,700 for everyone. When the FY 2014-2015 budget became law, the personal exemption became tiered, based on income level. The governor is proposing additional income tax cuts for low- and middle-income Ohioans by once again significantly increasing the state income tax personal exemption in Tax Year 2015.

<b>OHIO INCOME TAX PERSONAL EXEMPTIONS: ENACTED/PROPOSED</b>			
Income Level	Personal Exemption Before H.B. 483	Personal Exemption After H.B. 483	Personal Exemption After FY 16/17 Budget Proposal
\$0 – 40,000	\$1,700	\$2,200	\$4,000
\$40,000 – 80,000	\$1,700	\$1,950	\$2,850
\$80,000 +	\$1,700	\$1,700	\$1,700

*(TY 2016 indexing resumes)*

The higher exemptions under the governor’s proposal will actually eliminate all state income taxes for 200,000 more low-income Ohio households. All exemption thresholds will be adjusted for inflation beginning in Tax Year 2016.

## **FINANCING OHIO'S TAX CUT**

Unlike Ohio, a number of states are now struggling with projected budget deficits. Governor Kasich is proposing to deliver a half-billion dollar net tax cut with an approach that is fiscally responsible, balanced and structured to accelerate the economic progress Ohio has made the last four years. I've already mentioned the job growth, shrinking unemployment rate and empirical results demonstrating that what this governor and this General Assembly have done is working. But we have so much more potential that is being held back by a tax system in need of more reform. We can't fall behind as other states transform themselves to reflect today's economy. It's critical that we keep going, keep driving down income tax rates if we are to remain competitive. Other states are not standing still; they, too, are making changes to their tax structures (*see Attachment D*). If we allow people to keep more of their own money, they will make decisions as consumers that stimulate the economy and benefit the bottom lines of the companies that serve those consumers. Entrepreneurs and small business owners will get the message that Ohio has their back. What we can't do is give away the store and jeopardize the financial integrity of the state budget. That is why the governor is proposing to offset some of the foregone income tax revenues by raising the rates of some of the state's other taxes in a rational and reasonable fashion.

**Apply a Means-Test for Selected Income Tax Benefits:** I'd like to start by highlighting a change that is an important example of a rational change that helps preserve tax relief for those most in need. Under the proposal, a \$100,000 means test would be applied to five different income tax deductions and credits. More affluent taxpayers will no longer be eligible to claim these tax breaks: the \$50

senior credit, the retirement income credit, and the social security deduction, as well as the lump sum senior and retirement income credits. This proposal is included to help achieve a better balance of income tax cuts for Ohioans across all tax brackets.

**Align Taxes to Better Reflect and Grow Ohio's Economy:** A much more significant change in terms of revenue involves the effort to reduce Ohio's reliance on the anti-growth income tax by transitioning toward a more consumption-based tax system. The governor is proposing a one-half percent increase in the state sales tax rate, from 5.75 percent to 6.25 percent, and a small expansion of the sales tax base.

As you know, Ohio does not impose a sales tax on items most essential to our citizens, items like groceries, and prescriptions. That will not change. The change for consumers would amount to an additional 25 cents sales tax on a \$50 taxable purchase. As you can see in Attachment G, when the sales tax changes are combined with the income tax proposals, households receive an overall tax benefit. Consumer Expenditure Survey data was used to develop these estimates.

The change to the sales tax base means an expansion in the number of service-oriented businesses that would be required to charge sales tax. Keep in mind that services are taxed where the benefit is received, not where the service is performed. As some of you may know, in 1993, and again in 2003, the General Assembly approved base-broadening packages that made a number of services subject to sales tax. The first round of expansion made employment agencies, sports and fitness clubs, building maintenance and certain other services subject

to tax. The second expansion in 2003 brought satellite broadcasting, towing, dry cleaning and a few other services into the sales tax base.

With this budget, the governor is proposing to add five business types that primarily serve other businesses and three others that serve both businesses and households. Those that primarily service businesses include lobbying, public relations, market research and opinion polling, management consulting, and debt collection. Those serving both businesses and households include parking services, travel and pre-packaged tour agencies, and cable subscriptions.

Numerous interested parties have expressed concern about subjecting intercompany transactions to sales tax, specifically those services that are listed in R.C. Sec. 5739.01(B)(13)(d). We understand their viewpoints, and agree. It was not our intention to capture these intercompany transactions under the sales tax, and have language similar to that in R.C. 5739.01(B)(3)(e) to address this concern.

The governor and many tax policy analysts believe that these base broadening efforts strengthen the state's tax system by aligning the means of taxation with the growing consumption and services oriented economy (*see Attachment E*). For Ohioans it's important because it means they have a greater choice of how and when they'll be taxed. The Governor wants to have fewer tax dollars being withheld from paychecks, and instead give individuals the option of deciding whether they want to pay for a taxable good or service. There are other proposals, too, that will impact the sales tax base that I will discuss next.

**Reduce the Sales Tax Discount for Used Car and Watercraft Trade-Ins:** Ohio currently reduces the taxable sales price of a new car or boat by the full value of the car or boat being traded in by the buyer. This proposal would reduce that

discount to 50 percent. For a \$4,000 trade-in, with the 50 percent reduction and using the proposed higher sales tax rate, an individual will pay \$150 in additional state and local sales tax on a \$28,000 car. If the buyer finances the car over five years, that'll add about \$3 to the monthly payment.

**Reduce the Sales Tax Vendor Discount:** Since 1936, Ohio has allowed retail stores, restaurants and other sales tax vendors to keep a portion of all the sales tax they collect to cover expenses associated with reporting and remitting this tax. This vendor discount today is 0.75 percent. Of the 28 states that allow vendor discounts, 13 cap the amount that can be retained (*see Attachment F*). Today's automated technology makes compliance much easier and less costly. The governor is proposing to limit the discount to \$1,000 a month, joining other states that have adopted similar measures. This means smaller businesses will keep the full discount while big volume retailers – those doing over \$2 million in taxable sales a month – will no longer receive disproportionate compensation. Each year, some large vendors keep hundreds of thousands, even millions, of dollars from this discount. We are confident that their actual cost of collecting sales tax is a fraction of that amount, so the vendor discount paid with taxpayer dollars essentially functions as a profit center for those big retailers.

One hundred percent of Ohio income tax payers will have more disposable income if the governor's tax package is adopted (*see Attachment G*). Our state tax system allows approximately 20 percent of low-income households to pay no state income tax so cutting income taxes does not directly benefit those Ohioans. We estimate that the lowest income residents, those making less than \$15,000 a year and paying no income tax, will on average pay about \$34 extra a year in sales

tax as a result of the rate increase. We must not forget that lower income Ohioans are eligible for some very valuable benefits. The expansion of the Medicaid program by the governor is a good illustration of resources being provided lower income Ohioans. These residents may also be eligible for state-funded programs such as subsidized day care, educational grants, and early childhood education services. The basic necessities of life – groceries and prescription drugs – remain exempt from sales tax.

**Adjust the Commercial Activity Tax (CAT) Rate:** Since the CAT began in 2005, Ohio's only general business tax has stayed fixed at a rate of 0.26 percent. The proposal would adjust the rate to 0.32 percent while also reducing the minimum tax owed by businesses grossing between \$1 million and \$2 million from \$800 a year to \$150.

Large businesses in Ohio in the past ten years or so, have received some significant tax reductions with the elimination of the corporation franchise tax and the tangible personal property tax. Let me put it another way, since 2005, Ohio's larger businesses have seen their taxes cut by more than \$1 billion a year. Back then they paid about \$2.7 billion in corporation franchise tax and tangible personal property taxes. In 2014, businesses paid about \$1.7 billion in commercial activity tax. This proposed rate increase will push those payments up about \$400 million a year, but even at that, if you adjust the 2005 revenue figure for inflation, Ohio businesses after this CAT increase would still be paying about 40 percent less than they did ten years ago. Given that tax cut windfall for large businesses, the governor is asking that we balance that out and give some tax relief to small

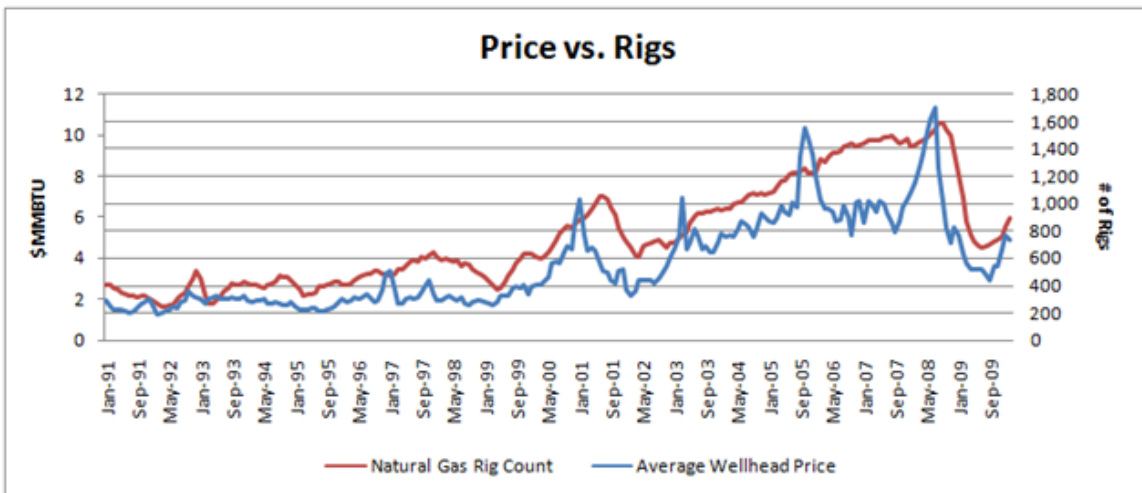
businesses, and doesn't think it's unreasonable to have large businesses help pay for it.

**Modernize Ohio's Oil and Gas Tax System:** There is another business that has enjoyed four years of very generous tax treatment from the state of Ohio. I'm talking, of course, about horizontal drilling and fracking that has been until recent years delivering just a trickle of natural gas and oil. Now horizontal drilling is capable of filling pipelines, particularly with natural gas, and it is time the people of Ohio share in the natural wealth of the state that is now flowing out of the ground underneath our feet. Unfortunately, much of that natural resource wealth is also flowing out of the state having paid very little severance tax, and no commercial activity tax. This mostly benefits drilling companies that are based outside Ohio and the contractors and employees they have brought in from Texas, Oklahoma and other states. Ohio has modernized its regulatory system to keep pace with these new drilling technologies; we should also modernize the tax system for natural gas and oil production, a system that was largely established 30 years ago.

Ohio's current severance tax has drilling companies paying just 20 cents on a barrel of oil and 3 cents on an MCF (thousand cubic foot) unit of natural gas. The calculation is based solely on volume, and does not incorporate the market value of the commodity. In addition, the current structure has no separate tax on natural gas liquids (NGLs), which are a highly valuable part of Ohio's new shale gas industry. Ohio's current severance tax structure has been a miniscule source of tax revenue for the state – the percent is 0.000192 – as you can see, it's a fraction of a fraction of one percent of our total general revenue. The governor proposes

fixed rates for crude oil and natural gas of 6.5 percent at the wellhead, and a lower rate of 4.5 percent for natural gas and NGLs when sold downstream. This lower rate is an allowance for the extra expense involved with transporting and processing the natural gas and NGLs.

It is the governor’s belief, and that of many others, that the industry will not leave the state simply because the tax rate rises to a level that is competitive with rates imposed by other states (*see Attachment H*). The decision to drill is certainly complex and unique to each company, but historically, drilling activity closely parallels the movement of the market price for natural gas and oil. When the price goes up, drilling increases; when it drops, drilling diminishes. If there is money to be made on the natural gas and oil resources available in Ohio, drillers will drill in Ohio.



(Source: U.S. Energy Information Administration, Baker Hughes, Inc.)

***The governor's tax proposal benefits local residents and all Ohioans.***

- All Ohioans will share in the benefits of the oil and gas boom in the form of lower income taxes.
- Royalty income to the property owners may qualify for the zero liability through the application of the Governor's small business investor income tax deduction proposal.
- Ohio's small, conventional natural gas producers will have severance taxes eliminated, meaning 90 percent of these wells in Ohio will pay no severance tax.
- State regulatory operations over oil and gas drilling will be funded first.
- Local communities impacted by horizontal drilling activities will receive 20 percent of the remaining severance tax revenue, an estimated \$20 million in the first year and then about \$40 million annually.

Of that 20 percent, half will be distributed to and through the county budget commissions for immediate local needs, with the first distribution occurring in November 2015. The Ohio Shale Gas Regional Commission, a nine-member board of local officials from the region and other industry-involved parties would be created and would control the other half of the severance tax revenue earmarked for local communities, with the following parameters. Of that, 50 percent would be available for infrastructure or other regional projects, and 50 percent will be deposited in a legacy fund to address and remedy long-term impacts from drilling, and would not be available for spending until 2025.

<b>NEW SEVERANCE TAX RATES ARE FAIR AND COMPETITIVE</b>			
<b>Product</b>	<b>Conventional Wells</b>	<b>High-Volume Horizontal Wells ("Shale Wells")</b>	
		<b>At Wellhead</b>	<b>Downstream*</b>
Crude Oil	20 cents per barrel ( <u>unchanged</u> )	6.5%	N/A
Natural Gas	<u>No tax</u> for wells less than 10 MCF/day, Wells more than 10 MCF/day, 3 cents/MCF	6.5%	4.5%
Natural Gas Liquids	Taxed as Natural Gas ( <u>unchanged</u> )	N/A	4.5%

*(\*Allowance for transportation and processing costs incorporated in the tax rate.)*

Let me anticipate and address a question that some of you are likely to ask. That is: with oil prices being so low, why would you raise the tax on the drilling industry? First, we need to remember that the Ohio shale play is primarily wet- and dry-gas, not oil. The market price associated with wet- and dry-gas has no direct correlation to the market price of oil. Second, in response to the question about the timing of a severance tax rate increase, I would ask another question: "What is most responsive to the interests of the people of Ohio, rather than the interests of mostly out-of-state natural gas and oil companies? Someone can

always argue that there is never a right time to fix Ohio's obsolete severance tax. The proposed tax changes will have little influence upon the decisions made by drilling companies; the price they can get for the product they extract will ultimately determine the level of drilling and extraction activity.

**Increase Tobacco Taxes:** Under this proposal, Ohio's cigarette tax would be increased from \$1.25 to \$2.25 per pack; the tax on Other Tobacco Products (OTP) would rise to a level equivalent to the cigarette tax. Public health agencies and other anti-smoking advocates argue that larger tax increases (similar to the governor's proposal of \$1.00 more per pack) have more impact on reducing the rate of smoking. There are some widely and long accepted studies showing higher cigarette and other tobacco product taxes will deter young people of all income levels from smoking (*see Attachment I*). Also, the revenue raised will help cover some of the public health expenses associated with smoking (e.g., Medicaid).

As I mentioned, the governor is also proposing to equalize the tax percentage of OTP tax on products like cigars, pipe tobacco, and chewing tobacco to a level comparable to cigarettes as a matter of equity. In addition, the governor is proposing a Vapor Products Tax, which would be imposed at a rate similar to those on cigarettes and OTP. Vaping and its associated paraphernalia is a relatively new phenomenon with a primary purpose of delivering nicotine to the user. ODT believes the proposal is an appropriate means of taxing this activity/product. Some will argue that e-cigarettes are a helpful way to quit smoking and, therefore, shouldn't be taxed. If the FDA approves e-cigarettes as a cessation method in the future, the proposed tax would no longer apply. The Centers for Disease Control and Prevention and the U.S. Food and Drug

Administration recently published a study showing that the use of e-cigarettes by middle and high school students tripled from 2013 to 2014. In fact, 13.4 percent of high school students currently use e-cigarettes, compared to 9.2 percent use of regular cigarettes. Increasing the price of the product is one proven strategy in reducing youth initiation to nicotine. The 2012 Surgeon General's report found that about three of every four teen smokers continue into adulthood.

There are two other changes that I need to mention. One, we would eliminate the 2.5 percent discount for timely payment of OTP tax. It shouldn't be necessary to reward businesses for paying their tax on time. Secondly, we are proposing to eliminate the 1.8 percent cigarette tax stamp discount in combination with defining a new formula for the calculation of cigarette minimum prices. By incorporating the tax into the minimum price calculation and eliminating the tax stamp discount, the state would save about \$20 million a year.

You can find a summary of the governor's tax proposal elements with the attachments accompanying this testimony (see Attachment J).

### **TAX EXPENDITURE REVIEW COMMITTEE**

I would now like to discuss a plan that, in our opinion, is long overdue. That is, conducting a comprehensive review of the 128 tax credits, exemptions, deductions, exclusions that apply to the various taxes that go into the state's GRF. These "tax expenditures" represent an estimated cost to the state as the foregone revenue of \$8.5 billion a year. The tax expenditures represent items that would normally be defined in a tax base. Unlike other general operating expenditures of the state that undergo biennial review and approval by the General Assembly during the budgetary process, these expenditures are typically

permanent, with little subsequent review to see if they are indeed satisfying the desired intent of the initial enactment of the tax expenditure.

Many of these tax expenditures have been in existence for decades. Some sales tax exemptions have been in existence since sales tax was adopted in the 1930s. We are proposing that a committee be created containing members of the legislative and executive branches, and the public. The current tax expenditures would be divided into four groups. The first group is to be reviewed in 2016 and the last group in 2019. The committee will issue an annual report by December 31st, recommending to the General Assembly whether each tax expenditure in the group should be retained, modified, or discontinued.

The committee would take a number of criteria into account when reviewing these tax expenditures. These may include who benefits, the fiscal impact, the public policy objective of the tax expenditure and could that objective be reached by more efficient means. In other words, are the tax credits and deductions doing their job? Do they contribute to a stronger local or state-wide economy? Do they help businesses grow or help provide quality jobs?

With that, Mr. Chairman, I conclude my testimony. Thank you again for the opportunity to share this information on the governor's proposals with you. I am certainly willing to take any questions your members may have.



## **ATTACHMENTS**

**A.ODT PRODUCTIVITY INCREASE**

**B.PASS-THROUGH ENTITIES BY SIZE OF GROSS RECEIPTS**

**C.ON INCOME TAX CUTS & ECONOMIC GROWTH**

**D.SUMMARY OF TAX CHANGES IN OTHER STATES**

**E.GROWTH OF CONSUMPTION-BASED ECONOMY**

**F.STATE SALES TAX RATES AND VENDOR DISCOUNTS**

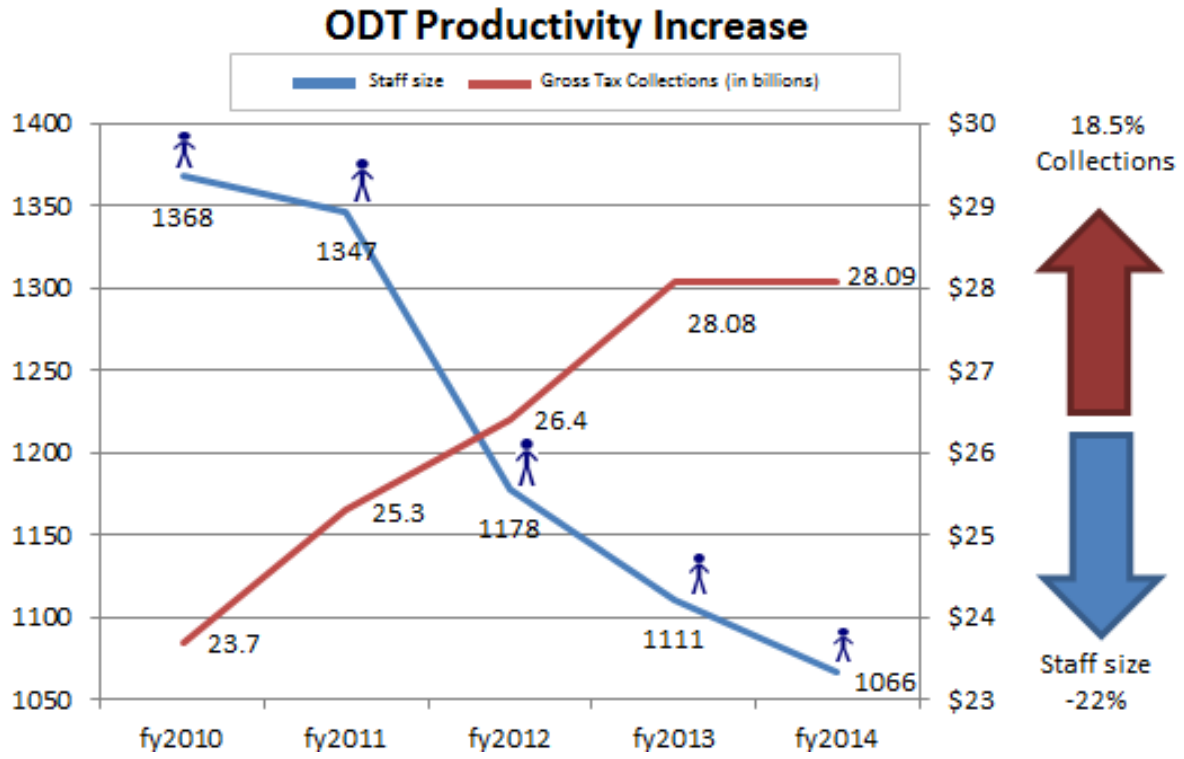
**G.CUMULATIVE ESTIMATED BENEFIT OF PROPOSED INCOME TAX REDUCTIONS AND SALES TAX INCREASES (2011-2016)**

**H.COMPARISON OF STATE SEVERANCE TAX RATES ON OIL AND NATURAL GAS / OHIO'S CURRENT AND PROPOSED RATES**

**I.STUDIES EXAMINING IMPACT OF TOBACCO TAX RATE ON SMOKING RATE**

**J.SUMMARY OF PROPOSED TAX REFORM ELEMENTS**

ATTACHMENT A: ODT PRODUCTIVITY INCREASE



**ATTACHMENT B: PASS-THROUGH ENTITIES BY SIZE OF GROSS RECEIPTS**

<b>COUNT OF TAX YEAR 2011 OHIO PASS-THROUGH BUSINESSES BY SIZE OF GROSS RECEIPTS</b>						
<b>Size of Gross Receipts</b>	<b>Number of Ohio Pass-Through Entities</b>	<b>Percent of total</b>	<b>Cumulative percent</b>	<b>Income</b>	<b>Percent of total</b>	<b>Cumulative percent</b>
\$2 million or less	1,033,672	98.30%	98.30%	\$11,789,550,846	42.80%	42.80%
\$2 million to \$4 million	7,948	0.80%	99.10%	\$1,363,843,655	4.90%	47.70%
\$4 million to \$10 million	5,544	0.50%	99.60%	\$1,888,510,497	6.80%	54.50%
\$10 million and above	4,400	0.40%	100.00%	\$12,534,418,184	45.50%	100.00%
<b>Total</b>	<b>1,051,564</b>			<b>\$27,576,323,182</b>		
<p>Source: IRS forms 1120S, 1065, 1040 Schedule C and Schedule F                      Income defined as Net Profit for Schedule C and Schedule F companies &amp; Ordinary Business                      Income for Partnerships and S-Corps</p>						

## ATTACHMENT C: ON INCOME TAX CUTS & ECONOMIC GROWTH

### Bibliography On Income Tax Cuts & Economic Growth

Arthur B. Laffer et al., *Rich States, Poor States ALEC-Laffer State Economic Competitiveness Index* (8<sup>th</sup> Ed. 2015)

Barry W. Poulson & Jules Gordon Kaplan, *State Income Taxes and Economic Growth*, 28 *Cato Journal* 53 (2008)

Donald Bruce & Tami Gurley, *Taxes and Entrepreneurial Activity: An Empirical Investigation Using Longitudinal Tax Return Data*, 252 *Small Business Administration* 1 (2005)

Mark Rider, *The Effect of Personal Income Tax Rates on Individual and Business Decisions – A Review of the Evidence* 1 (International Studies Program Working Paper 06-15, 2006)

Mark Rider, *Can Georgia Adopt a General Consumption tax*, (Georgia State University, Fiscal Report Center 235, 2011)

Randall G. Holcombe & Donald J. Lacombe, *The Effect of State Income Taxation on Per Capita Income Growth*, 32 *Public Finance Review*, 292 (2004)

Andrew Lai, Roger Cohen & Charles Steindel, *The Effects of Marginal Tax Rates on Interstate Migration in the U.S.* (New Jersey Dep't of the Treasury, 2011)

Ergete Ferede & Bev Dahlby, *The Impact of Tax Cuts on Economic Growth: Evidence from the Canadian Provinces*, 65 *National Tax Journal* 563

Robert Reed, *The Robust Relationship Between Taxes and U.S. State Income Growth*, 61 *National Tax Journal* 57-80 (2008)

Marc Tomljanovich, *The Role of State Fiscal Policy in State Economic Growth*, 22 *Contemporary Economic Policy* 318-330 (2004)

## **ATTACHMENT D: SUMMARY OF TAX CHANGES IN OTHER STATES**

States continue to enact significant tax rate changes.

Alaska, Florida, Nevada, South Dakota, Texas, Washington, and Wyoming continue to impose **zero** personal income tax.

### **Arkansas**

The Arkansas personal income tax rates fell by 0.1% for taxpayers earning less than \$4,100 in tax year 2014 and for all others beginning in tax year 2015. Ark. Code Ann. 26-51-201(a); 201(d).

### **Arizona**

Arizona is phasing down its corporate income tax rate. The rate fell to 6.5% from 6.968% for tax year 2014. It will further fall to 6% in tax year 2015, 5.5% in tax year 2016, and 4.9% in subsequent tax years. Ariz. Rev. State Ann. 4.3-1111.

### **Illinois**

Illinois' corporate income tax rate fell from 7.0% in tax year 2014 to 5.25% in tax year 2015. ILCS 5/201(b)(12).

Illinois personal income tax rate fell from 5% in tax year 2014 to 3.75% in tax year 2015. ILCS 5/201(b)(5.2).

### **Indiana**

Indiana is phasing down its corporate income tax rate. The rate fell from 7% to 6.5% after 6/30/2014 and will continue to fall to 4.9% after 6/30/2021. Ind. Code 6-3-2-1(B); 6-3-2-1.5(b).

Indiana's flat personal income tax rate fell from 3.4% in tax year 2014 to 3.3% in tax year 2015. Ind. Code 6-3-2-1.

### **Kansas**

Kansas' top personal income tax rate fell from 6% in tax year 2013 to 4.8% in tax year 2014 and fell again to 4.6% in tax year 2015. Kan. Stat. Ann. 73-32, 110(a)

### **Massachusetts**

Massachusetts personal income tax rate fell from 5.25% in tax year 2013 to 5.20% in tax year 2014 and fell again to 5.15% in tax year 2015. Mass. Gen. L. Chapter 62 § 4.

### **North Carolina**

North Carolina's corporate income tax fell from 6.9% in tax year 2013 to 6% in 2014 and fell again to 5% in tax year 2015. N.C. Gen. State 105-130.3.

North Carolina's income tax fell from a range of 6% to 7.75% in tax year 2013 to a flat 5.8% in tax year 2014 and that flat rate fell again to 5.75% in tax year 2015.

### **Rhode Island**

Rhode Island's corporate income tax rate fell from 9% in tax year 2014 to 5% in tax year 2015. R.I. Gen. Laws 44-11-2.

### **South Carolina**

South Carolina's lowest marginal personal income tax rate fell from 3% in tax year 2013 to 2.5% in tax year 2014. S.C. Code Ann. 12-6-510(A)

### **Texas**

Texas's margin tax rate declines from 1% of taxable margin for entities with revenues of \$1,030,000 or more in tax year 2013 (0.5% of taxable margin for taxable entities primarily engaged in retail or wholesale trade) to 0.975% of taxable margin for entities with revenues of \$1,080,000 or more in tax year 2014 (0.4875% of taxable margin for taxable entities primarily engaged in retail or wholesale trade), to 0.95% of taxable margin in tax year 2015 (0.475% of taxable margin for taxable entities primarily engaged in retail or wholesale trade). Tex. Tax Code Ann. 171.002; Tex. Tax Code Ann. 171.0023.

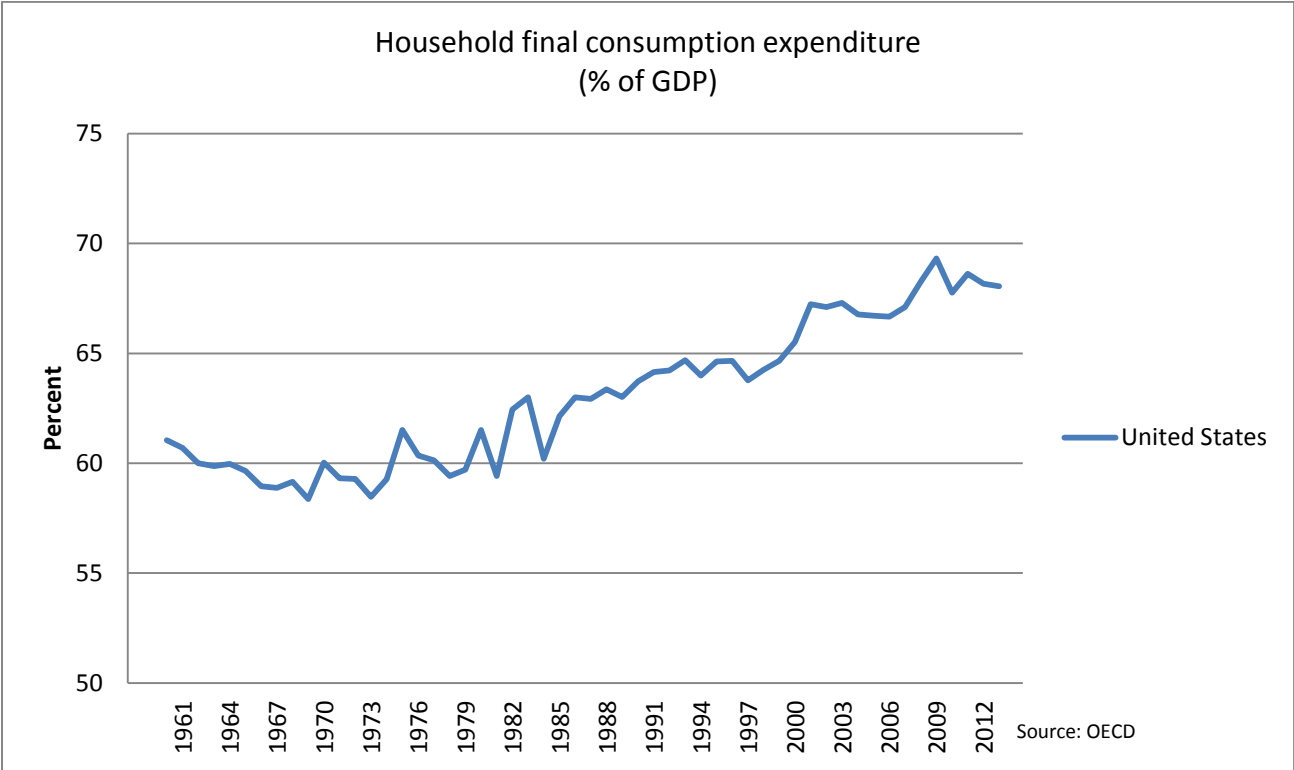
### **Wisconsin**

Wisconsin's lowest marginal personal income tax rate fell from 4.40% in tax year 2013 to 4.0% in tax year 2014. Wis. Stat. 71.06(1q).

### **West Virginia**

West Virginia's corporate income tax fell from 7% in tax year 2013 to 6.5% in tax years 2014 and thereafter. W.Va. Code 11-24-4(8).

**ATTACHMENT E: GROWTH OF CONSUMPTION-BASED ECONOMY**



ATTACHMENT F

**STATE SALES TAX RATES AND VENDOR DISCOUNTS**

(January 1, 2015)

	STATE SALES		VENDOR	
STATE	TAX RATE	RANK	DISCOUNT	MAX/MIN
ALABAMA	4.0%	39	5.0%-2.0% (1)	\$400/month (max)
ALASKA	----- -----	-----N/A----- -----	----- -----	
ARIZONA	5.6%	28	1.0%	\$10,000/year (max)
ARKANSAS	6.5%	9	2.0%	\$1,000/month (max)
CALIFORNIA	7.50%	1	None	
COLORADO	2.9%	46	3.33% (4)	
CONNECTICUT	6.35%	11	None	
DELAWARE	----- -----	-----N/A----- -----	----- -----	
FLORIDA	6.0%	16	2.5%	\$30/report (max)
GEORGIA	4.0%	39	3.0%-0.5% (1)	
HAWAII	4.0%	39	None	
IDAHO	6.0%	16	None (5)	
ILLINOIS	6.25%	12	1.75%	\$5/year (min)
INDIANA (2)	7.0%	2	0.73% (2)	
IOWA	6.0%	16	None	
KANSAS	6.15%	15	None	

KENTUCKY	6.0%	16	1.75%-1.5% (1)	\$50/month (max)
LOUISIANA	4.0%	39	0.935%	
MAINE	5.5%	29	None (5)	
MARYLAND	6.0%	16	1.2%-0.90% (1)	\$500/return (max)
MASSACHUSETTS	6.25%	12	None	
MICHIGAN	6.0%	16	0.5% (6)	\$6/month (min), \$15,000/month (max)
MINNESOTA	6.875%	7	None	
MISSISSIPPI	7.0%	2	2.0%	\$50/month (max)
MISSOURI	4.225%	37	2.0%	
MONTANA	----- -----	-----N/A----- -----	----- -----	
NEBRASKA	5.5%	29	2.5%	\$75/month (max)
NEVADA (9)	6.85%	7	0.25%	
NEW HAMPSHIRE	----- -----	-----N/A----- -----	----- -----	
NEW JERSEY	7.0%	2	None	
NEW MEXICO	5.125%	31	None	
NEW YORK	4.0%	39	5.0%	\$200/quarter (max)
NORTH CAROLINA	4.75%	34	None	
NORTH DAKOTA	5.0%	32	1.5%	\$110/month (max)
OHIO	5.75%	26	0.75%	
OKLAHOMA	4.5%	36	1.0%	2,500/month (max)

OREGON	----- -----	-----N/A----- -----	----- -----	
PENNSYLVANIA	6.0%	16	1.0%	
RHODE ISLAND	7.0%	2	None	
SOUTH CAROLINA	6.0%	16	3.0%-2.0% (1)	\$3,100/year (max)
SOUTH DAKOTA	4.0%	39	1.5% (10)	
TENNESSEE	7.0%	2	None	
TEXAS	6.25%	12	0.5% (7)	
UTAH (3)	4.7%	34	1.31%	
VERMONT	6.0%	16	None (5)	
VIRGINIA (3)	4.3%	37	1.6%-0.8% (8)	
WASHINGTON	6.5%	9	None	
WEST VIRGINIA	6.0%	16	None	
WISCONSIN	5.0%	32	0.5%	\$10/period (min)
WYOMING	4.0%	39	1.95%-1.0% (1)	
DIST. OF COLUMBIA	5.75%	26	None	
U. S. MEDIAN	5.75%			28 states allow vendor discounts

Source: Compiled by FTA from various sources.

(1) In some states, the vendors' discount varies by the amount paid. In AL and SC, the larger discounts apply to the first

\$100. In GA, the larger discount applies to the first \$3,000. In KY, the larger discounts apply to the first

\$1,000, while MD applies the larger discount to annual collections of \$6,000. In WY, the larger discount applies to the first \$6,250.

The lower discounts apply to the remaining collections above these amounts.

(2) Utilities are not permitted to take discount. Collection allowances are 0.73% if total sales tax collected is less than

\$60,000; 0.53% if total taxes are between \$60,000 and \$600,000; 0.26% if total sales tax collected is more than \$600,000.

(3) Rate does not include a statewide local rate of 1.0% in VA and 1.25% in UT. In UT, a discount of 1% is applicable to local taxes.

(4) Local option sales tax discount varies from 0% to 3.33%.

(5) Vendors are allowed to keep any excess collections prescribed under the bracket system.

(6) Vendor discount only applies to the first 4.0% of the tax. A 0.75% discount if paid by the 12th of the month.

(7) An additional discount of 1.25% applies for early payment.

(8) Discount varies; 1.1% (1.6% for food) of the first \$62,500, 0.84% (1.2%) of the amount to \$208,000, and 0.56% (0.8%)

of the remainder. Applies to the state tax only. No discount allowed on electronically file returns.

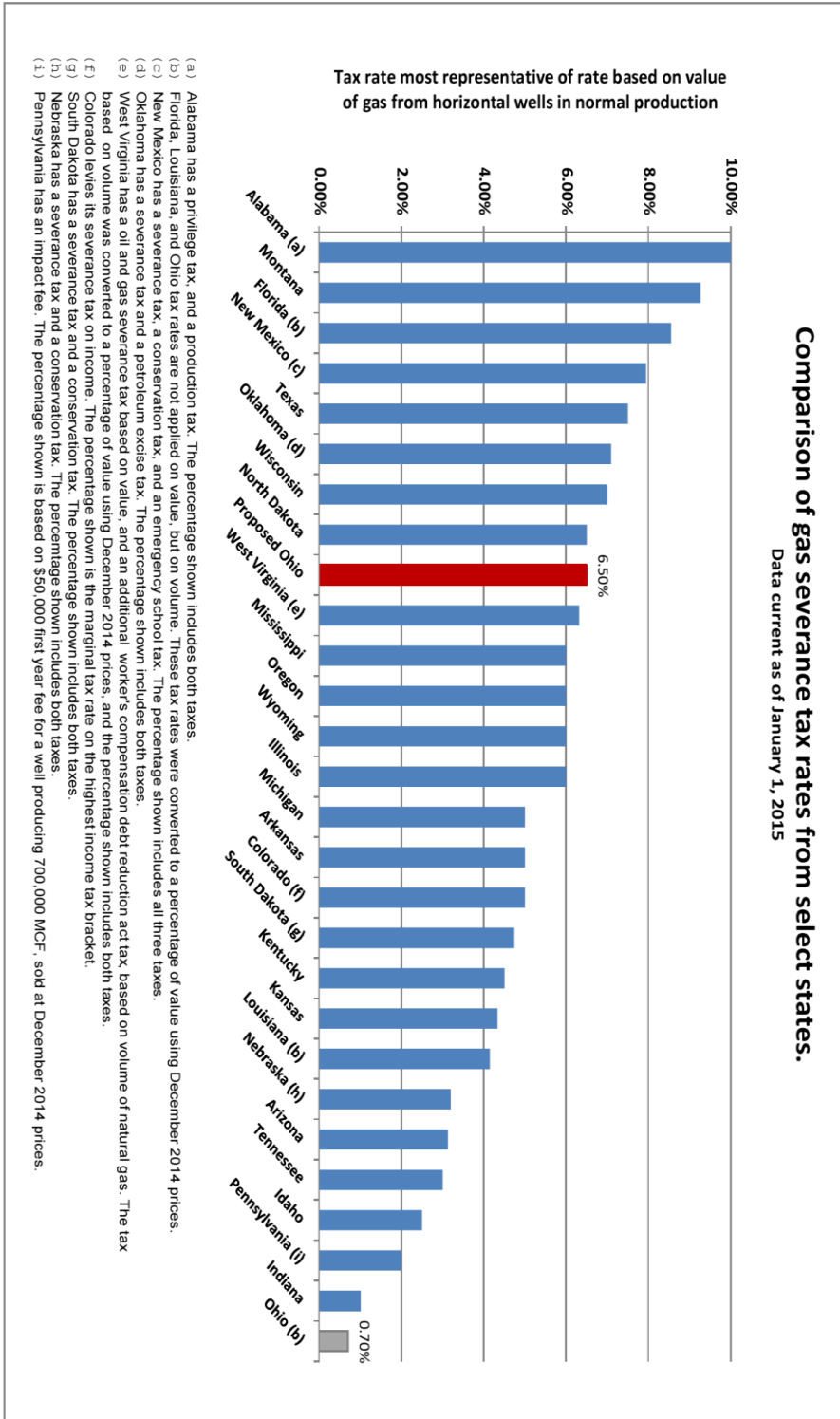
(9) Sales tax rate in NV will fall to 6.5% on 7/1/15.

(10) Electronic Filers only.

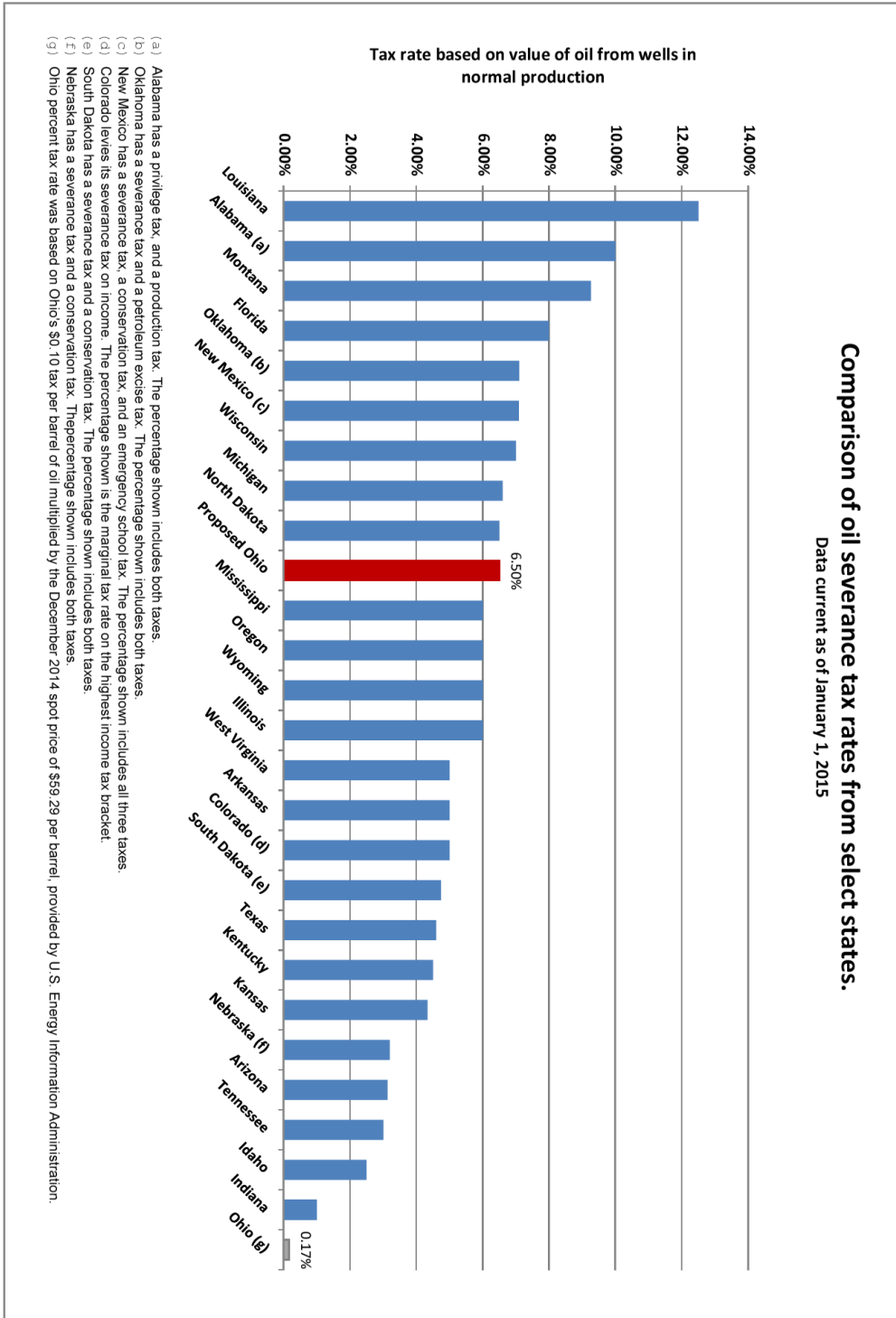
**ATTACHMENT G: CUMULATIVE ESTIMATED BENEFIT OF PROPOSED INCOME TAX REDUCTIONS  
AND SALES TAX INCREASES (2011-2016)**

Cumulative Benefit of Income Tax Reductions and Sales Tax Increases (2011 – 2016)										
Taxpayer	Annual Income	Income Taxes Due for CY2011	Income Taxes Due for CY2016	Total Income Tax Reduction 2011-2016	Income Tax Percent Reduction	Estimated State Sales Tax Liability CY 2011 <sup>3</sup>	Estimated State Sales Tax Liability CY 2016 <sup>3</sup>	Estimated Increase in State Sales Tax <sup>4</sup>	State Sales Tax Percent Increase	Net Change in Taxes
Single	\$14,100	\$122.64	\$0.00	<b>(\$122.64)</b>	-100.00%	\$202.00	\$229.00	\$27.00	13.37%	<b>(\$55.64)</b>
Single	\$20,000	\$276.78	\$130.92	<b>(\$147.86)</b>	-53.04%	\$240.00	\$272.00	\$32.00	13.33%	<b>(\$115.86)</b>
Single parent w/ two children <sup>1</sup>	\$30,000	\$462.38	\$0.00	<b>(\$462.38)</b>	-100.00%	\$840.00	\$953.00	\$113.00	13.45%	<b>(\$349.38)</b>
Single (median income) <sup>2</sup>	\$41,000	\$1,005.89	\$689.29	<b>(\$336.60)</b>	-33.46%	\$270.00	\$307.00	\$37.00	13.70%	<b>(\$299.60)</b>
Single	\$50,000	\$1,366.88	\$907.43	<b>(\$459.45)</b>	-33.61%	\$374.00	\$425.00	\$51.00	13.64%	<b>(\$408.45)</b>
Married filing joint w/ no children	\$60,000	\$1,520.98	\$997.36	<b>(\$523.62)</b>	-34.43%	\$692.00	\$787.00	\$95.00	13.73%	<b>(\$428.62)</b>
Married filing jointly w/ one child (median income) <sup>2</sup>	\$60,000	\$1,441.96	\$921.76	<b>(\$520.20)</b>	-36.08%	\$935.00	\$1,063.00	\$128.00	13.69%	<b>(\$392.20)</b>
Married filing joint w/ two children (median income) <sup>2</sup>	\$73,000	\$1,843.70	\$1,179.31	<b>(\$664.39)</b>	-36.04%	\$1,409.00	\$1,601.00	\$192.00	13.63%	<b>(\$472.39)</b>
<sup>1</sup> eligible for OH Earned Income Tax Credit										
<sup>2</sup> Median incomes are from 2011 data.										
<sup>3</sup> Estimated based upon Consumer Expenditure Survey Data and Ohio Department of Taxation calculations. Sales tax liability estimates are controlled for inflation to show results from rate increase only.										
<sup>4</sup> Includes increases in state sales tax rates in October 2013 and proposed for October 2015.										
2/9/2015										

**ATTACHMENT H: COMPARISON OF STATE SEVERANCE TAX RATES ON OIL AND NATURAL GAS / OHIO'S CURRENT AND PROPOSED RATES (1 of 2)**



**ATTACHMENT H: COMPARISON OF STATE SEVERANCE TAX RATES ON OIL AND NATURAL GAS / OHIO'S CURRENT AND PROPOSED RATES (2 of 2)**



## ATTACHMENT I: STUDIES EXAMING IMPACT OF TOBACCO TAX RATE ON SMOKING RATE

### Bibliography Taxes & Tobacco Use

Congressional Budget Office, *Raising the Excise Tax on Cigarettes: Effects on Health and the Federal Budget* (2012)

Centers for Disease Control and Prevention, *Health Effects of Cigarette Smoking* (2014)

Centers for Disease Control and Prevention, *Smokeless Tobacco: Health Effects* (2014)

Natalie McGill, *Research on E-cigarettes Examining Health Effects: Regulations Due*, 43 *The Nation's Health* 1 (2013).

F.J. Chaloupka et al., *Tax, Price, and Cigarette Smoking: Evidence from the Tobacco Documents and Implications for Tobacco Company Marketing Strategies*, 11 *Tobacco Control* 62 (2002)

John A. Tauras et al., *Effects of Price and Access Laws on Teenage Smoking Initiation: A National Longitudinal Analysis* (2001)

Frank J. Chaloupka and Rosalie Liccardo Pacula, *An Examination of Gender and Race Differences In Youth Smoking Responsiveness to Price and Tobacco Control Policies* (Nat'l Bureau of Econ. Research, Working Paper No. 6541, 1998)

Sherry Emery et al., *Does Cigarette Price Influence Adolescent Experimentation*, 20 *Journal of Health Economics* 261 (2000)

Matt Richtel, *Selling a Poison by the Barrel: Liquid Nicotine for E-Cigarettes*, *N.Y. Times* March 23, 2014, at A1

Centers for Disease Control and Prevention, *E-cigarette use triples among middle and high school students in just one year*, April 16, 2015 news release

**ATTACHMENT J: SUMMARY OF PROPOSED TAX REFORM ELEMENTS**

Tax Reform Table	State - All Funds		Local		Net Overall Cut	
	FY2016	FY2017	FY2016	FY2017	FY2016	FY2017
<u>Cuts</u>						
Income tax across the board -15% -23%	(1,392.8)	(2,240.3)				
Withholding rate cuts to match tax rates	(636.3)	(358.2)				
Eliminate income tax for businesses <= \$2 million	(337.8)	(358.2)				
Personal exemption increase for \$0 - \$40,000 group	(98.4)	(98.4)				
Personal exemption increase for \$40,000 - \$80,000 group	(85.6)	(89.6)				
Lower CAT annual minimum tax for businesses \$1 million - \$2 million	(15.0)	(14.5)				
Subtotal:	(2,565.9)	(3,159.2)				
<u>Increases</u>						
Means test social security deduction for \$100,000+ group	126.2	138.2				
Means test senior and retirement tax credits for \$100,000+	25.7	28.3				
State sales tax rate from 5.75% to 6.25%	689.4	949.2				
Expand sales tax on some B2B services (see below)	265.0	299.7	59.4	68.0		
Expand sales tax to cable subscriptions, parking, travel	87.3	105.5	19.6	23.8		
Reduce MV and watercraft trade in credit to 50%	73.8	101.6	17.2	24.3		
Cap vendor discount at \$1,000 per month	21.1	29.6	4.9	5.2		
CAT rate from 0.26% to 0.32%	304.7	416.2				
Severance 6.5% at wellhead, 4.5% downstream	76.5	183.4	19.1	45.8		
Cigarette tax from \$1.25 to \$2.25 per pack (+ floor tax in 2016)	415.0	337.1				
Equalize tax on other tobacco products, e-cigs & vapor	89.9	102.5				
Eliminate payment discounts - cigarettes, OTP & beer and wine	24.7	24.5				
Subtotal:	2,199.3	2,715.8	120.2	167.1		
Net:	(366.6)	(443.4)	120.2	167.1	(246.4)	(276.3)
B2B services:						
Mgmt consulting/public relations						
Market research/opinion polling						
Lobbying						
Debt collection						