TESTIMONY OF RICHARD VEDDER,
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**Chairman Edwards and members of the committee. I am here to testify in favor of one component of this year's budget, namely a major reduction in the Ohio personal income tax. I am an emeritus distinguished professor of economics at Ohio University who wrote my first article on state and local government finance 60 years ago for the state of Illinois. I have worked and consulted for the Joint Economic Committee of Congress, and have testified numerous times before Congress, the European Parliament, the Ohio General Assembly, other state legislatures, and have consulted on economic affairs with political leaders throughout the world, for example Russia's Vladimir Putin and Israel's Benjamin Netanyahu. Governor DeWine has appointed me to the Ohio Economic Roundtable, advising the Office of Budget and Management. With me today is Nathan Bilski, an Honors Tutorial Student in finance soon graduating from Ohio University and then taking a great job with one of Wall Street's leading firms. Nate's excellent thesis research helped in preparing my remarks. Both Nate and I are here as citizens, not paid by anyone, including Ohio University, who probably would have preferred that we not come.**

**The economic dilemma facing humans is that our wants exceed our ability to fulfill them, so anytime governments expend resources, that typically forces them to reduce spending on other desired activities. While governments can finance spending in numerous ways, including borrowing, receiving federal grants, selling assets, enacting user fees, using eminent domain or, for the federal government even printing money, most state activities are appropriately financed through taxation.**

**A "good tax" has four attributes. It is cheap to administer and easy to understand, does little harm to the economy by not distorting market-driven uses of resources, is perceived as being fair and equitable, and is transparent –readily seen by the taxpaying public. Of these criteria, the one that is most disputed is the fairness one ---what some might view as grossly unfair, others perceive as fair and just.**

**I have read news accounts suggesting you have been having fun spending money like drunken soldiers, but I assume this is mostly one-time federal money and that state fiscal conditions still remain relatively strong, suggesting that there is room for a sizable tax reduction. The fiscal note issued by the Legislative Service Commission underscores that. House Bill 1 also materially involves property taxation. While I have some ideas about that, Nate and I will confine our testimony to Job One, repairing the income tax in Ohio.**

**Ohio is facing what I would call a growth deficit: the rate of growth in income and output, even correcting for population change, has typically been lower than the national average. See Table 1. In 1929, right before the Great Depression, Ohio's personal income per capita was 10.5 percent above the national average –we were considered a highly prosperous state. By 1950, Ohio's income advantage had declined a bit, and beginning in the mid-1970s we fell below the national average. That income deficit grew rather consistently into this century. For example, in 2010, Ohio personal income per capita was 9.3 percent below the national average, and while the *rate of decline* has slowed considerably, in 2021 we were sadly 11.3 percent below the national average. Relative to the nation as a whole, over the last century Ohio has had a somewhat sluggish**

**economy. It seems to me that *the single most important goal for Ohio government is to end and reverse that erosion in our material abundance relative to other states*.**

**The state's tax, expenditure and regulatory policies all impact our economic standing and, more generally, the quality of our life. One can argue that the ultimate measure of Ohio's success is not so much our income levels but our overall attractiveness as a state, probably best measured by net migration: are people moving into or out of Ohio? There too the record is discouraging, as more native-born Americans are leaving the Buckeye State than moving in. Just ask U-Haul. It costs 72 percent more to rent a 26 foot long U Haul truck leaving today, March 28, going from Cleveland to Austin, Texas than to rent one making the *exact same trip* in the opposite direction. Why? Lots of people want to go to Austin, which thereby accumulates lots of trucks. Few people want to move to Cleveland. From July 1, 2021, to June 30, 2022, the population of Ohio FELL by 8,284, while that of Texas ROSE by 470,708. That stark difference was NOT because Texans are better lovers than Ohioans, but predominately because people are moving into Texas in large numbers, but not into Ohio.**

**The evidence shows people like states with a low or no income tax. Texas, Florida, Tennessee, Nevada and Washington state all have significant in-migration, and they *all* have the ultimate flat rate income tax –one with a *zero* rate. New York, California and New Jersey all have highly progressive income taxes, with some residents paying over 10 percent of increases in income in higher state taxes. *All* have substantial out-migration of people. To cite two famous examples, Elon Musk moved from California to Texas and billionaire venture capitalist Ken Griffin moved from Illinois to Florida –saving millions annually in taxes.**

**Using multivariate statistical techniques, specifically regression analysis, Nate and I found that, controlling for some other relevant migration factors, people prefer living in states with low aggregate levels of state and local income taxation. More broadly, population growth is greater in relatively low income tax states. Also, we found that the growth in income over time tends to be greater in states with lower income taxation.**

**Recognizing this empirical reality, many states have recently moved from highly progressive to flat rate income taxes with a relatively low marginal rate. The *Wall Street Journal* reports 23 states have cut income taxes since 2021. In the Midwest, the best example is Iowa, which is in the process of moving from an income tax with a top rate in 2022 of 8.98 percent to a flat rate tax with a 3.9 percent rate by 2026 – slightly lower than Ohio's top rate. The chief competitor of ours for Intel's huge semiconductor chip investments is Arizona, a state that recently moved from a progressive income tax to one with a forthcoming flat rate of just 2.5 percent. Don't be surprised if they don't scale back their announced Ohio investments while maintaining those in Arizona.**

**Perhaps most relevant is the behavior of neighboring states. *Every single state bordering Ohio except West Virginia has moved to a flat rate income tax, and even West Virginia this year has adopted a tax reduction in its top rate of over 20 percent. Indiana, Michigan, Pennsylvania and Kentucky have all adopted a flat rate income tax, some with rates well below our top rate of 3.99 percent.* The only state in the Union bucking the trend and moving from flat rate to progressive income taxation is Massachusetts, and I would bet you, Chairman Edwards, a dinner at the Rhapsody Restaurant in your magnificent hometown of Nelsonville that the Bay State will soon**

**start facing a big exodus of its wealthiest and generally most productive citizens to no income tax havens like Miami, Nashville and Austin.**

**Actually, I have *understated* Ohio's tax disadvantage. The data on just state income taxes ignores another disadvantage facing Ohio. We have unusually high *local* income taxes, probably because I believe we are the only state in the Union with widespread *school district* income taxation. While the top Ohio marginal income tax rate is currently advertised as being a fairly reasonable 3.99 percent, in reality many residents of the Buckeye State currently face a marginal tax rate of over six percent because of high municipal and school district taxes.**

**In light of that, even after achieving a 2.75 percent top rate on the state income tax, the Buckeye State would not have a lower marginal rate than neighboring states like Indiana when local taxes are included. Therefore, the optimal strategy would call for *further* reductions in the income tax that would take effect if state revenue and fund balances remained at prudent levels. For example, one could talk about annual 0.25 percent reductions in the top rate until by 2035 the income tax would be eliminated.**

**As suggested earlier, there are different perspectives on the fairness of taxes. Some argue that rich persons should pay not only more dollars in taxes, but also a larger *proportion* of their income. This argument, however, must also consider that state and local income taxes are *far* less important than federal taxes, and our federal tax system is *extremely* progressive, with the top one percent in terms of income paying over 42 percent of federal income taxes in 2020. Also, I would note that income inequality in Ohio is far lower than in states with highly progressive income taxes, most notably**

**New York and California. Ohio is sadly lacking lots of billionaires, having only seven of the 735 American billionaires according to *Forbes* Magazine –dramatically fewer, adjusting for population, than the national average.**

**Clergy, college professors and, yes, politicians, have one common failing –we all talk too much, and the law of diminishing returns applies to us like anyone else. So it is best I simply say, "thank you for listening."**