

# **ETPI**

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## **Ohio's Tax Ranking: Setting the Record Straight**

### **Introduction**

Each year, stories appear in the media highlighting the latest round of tax comparisons among the fifty states. Given the complexity of state and local taxes, it seems helpful to know in a few summary figures how Ohio tax levels compare with others. Ordinarily, they show Ohio's taxes as fairly average, ranking about in the middle among the states.

Several organizations publish such annual rankings. This year, one of them declared that Ohio has the third highest taxes in the nation. Perhaps due to the novelty of this conclusion, made by a national group called the Tax Foundation, it has attracted considerably more attention in Ohio than rankings made by other organizations. It is often cited by legislators or referred to in news stories and letters to the editor.

Fortunately for Ohio taxpayers, the Tax Foundation rankings are not accurate, at least not by standard and generally accepted methods of comparison. Ohio does not rank as a high-tax state. It remains fairly close to average. The purpose of this report is to set the record straight on Ohio's tax levels and ranking among the states.

### **Report Answers Six Questions**

This report answers six key questions about comparative state tax rankings:

- (1) What is the data source for state and local tax comparisons?
- (2) Who makes comparisons and how are they made?
- (3) How does Ohio rank in the latest round of standard comparisons?
- (4) How do the Tax Foundation rankings compare to all the others?
- (5) Why are the Tax Foundation rankings so different from all the others?
- (6) What is the contribution of *local* taxes to Ohio's tax ranking?

The next six sections of the report address each of these questions, in turn.

## **What is the Data Source for State and Local Tax Comparisons?**

Virtually all comparisons of total state and local tax burdens use the same data source: the U.S. Census Bureau. Because it is a Herculean task to collect and compile data for 50 states and over 80,000 local units of governments (municipalities, counties, townships, school districts, and special districts), the Census Bureau is the only reliable source.

The most current and complete information to compare state and local tax collections was issued in January 2003 (but see next paragraph for a note). For state governments, the figures represents fiscal year 2000, which in most states began on July 1, 1999 and ended on June 30, 2000. For local governments, the figures most often represent calendar year 1999. The data is available on the web at [www.census.gov](http://www.census.gov).

(Note: as this report was undergoing final editing, the Census Bureau released FY 2002 “preliminary” state and local data, after making a decision not to publish FY 2001, skipping a year of local data collection to help accelerate publication of the state and local information. Only one of the four organizations cited below has prepared new figures based on the preliminary data and it is unlikely that Tax Foundation will revise their numbers since they already are intended to represent a later time period than the preliminary Census figures. Consequently, this ETPI report will not attempt to incorporate or discuss the preliminary Census data. An updated ETPI report may be prepared when more complete information becomes available.)

## **Who Makes Comparisons and How Are They Made?**

Since the Census Bureau data are available on the Internet, anyone who has the necessary expertise is able to make comparisons and then rank the states. This report cites rankings prepared by four respected organizations to contrast with the Tax Foundation figures. Two are national groups and two are in Ohio. They are:

- Federation of Tax Administrators (FTA)
- Congressional Quarterly (State Fact Finder, 2004)
- Ohio Department of Taxation
- Ohio Public Expenditure Council (OPEC)

## Who Makes Comparisons and How Are They Made? (continued)

A little background about each of these four organizations or sources may be useful. The Federation of Tax Administrators, or FTA, is the membership organization for state departments of revenue. Located in Washington, D.C., it is professional, non-partisan, nationally respected, and widely known. Public officials and the news media routinely cite their figures. Their web address is [www.taxadmin.org](http://www.taxadmin.org).

A second national and highly respected source is “CQ’s State Fact Finder 2004, *Rankings Across America*” a paperback publication of Congressional Quarterly, Inc., also in Washington, D.C.

In Ohio, the state department of taxation publishes an annual data series containing the state comparisons. Their figures are available on the department’s excellent website at [www.ohio.gov/tax](http://www.ohio.gov/tax). A private sector taxpayer organization, the Ohio Public Expenditure Council (OPEC) also makes figures available in a published paperback report called “Ohio Tax Climate.” Each of these four sources will be referred to later in this report.

Each organization compiles its state rankings similarly, starting with the Census Bureau data for state and local tax collections in each state. These collection figures must then be divided by an appropriate measure to validly compare states. There are two standard methods of comparison. The first is per capita tax collections, which are computed simply by dividing each state’s tax collection figure by its population.

The other measure divides tax collections by the state’s total personal income. The resulting figure is expressed in terms of taxes as a percentage of income. Both measures are widely used and all four of the organizations cited above publish both measures for all states. Rather than bore the reader with a series of virtually identical tables, the state-by-state figures are shown here only from the FTA, since that organization is often considered to be the single most authoritative source for the comparisons.

Both of the 50-state tables shown on the next few pages of this report display state and local taxes combined, rather than separating state taxes from local taxes. Although the separate figures are readily available, public finance experts agree that for most purposes the state and local totals better represent comparative tax levels among states. The final section of this report does contain comparisons between Ohio and national averages for state taxes alone and for local taxes alone so that the contribution of local taxes to the overall rankings can be assessed.

## How Does Ohio Rank in the Latest Standard Comparisons?

Ohio's per capita state and local taxes were \$3,016 in FY 2000, ranking Ohio 20<sup>th</sup> among the fifty states. Figures for all fifty states are shown below.

### Ohio Ranks 20<sup>th</sup> in State and Local Taxes Per Capita

<u>Rank</u>	<u>State</u>	<u>Per Capita Taxes</u>	<u>Rank</u>	<u>State</u>	<u>Per Capita Taxes</u>
1	Connecticut	\$ 4,595	26	Kansas	\$ 2,833
2	New York	\$ 4,578	27	Iowa	\$ 2,765
3	New Jersey	\$ 3,903	28	North Dakota	\$ 2,754
4	Massachusetts	\$ 3,787	29	Oregon	\$ 2,751
5	Minnesota	\$ 3,694	30	Indiana	\$ 2,691
6	Alaska	\$ 3,687	31	North Carolina	\$ 2,664
7	California	\$ 3,545	32	New Hampshire	\$ 2,652
8	Wisconsin	\$ 3,458	33	New Mexico	\$ 2,639
9	Maryland	\$ 3,454	34	Utah	\$ 2,630
10	Hawaii	\$ 3,384	35	Florida	\$ 2,624
11	Maine	\$ 3,343	36	Arizona	\$ 2,599
12	Delaware	\$ 3,340	37	Missouri	\$ 2,558
13	Rhode Island	\$ 3,256	38	Idaho	\$ 2,546
14	Illinois	\$ 3,241	39	Kentucky	\$ 2,517
15	Washington	\$ 3,178	40	Texas	\$ 2,505
16	Michigan	\$ 3,167	41	Louisiana	\$ 2,436
17	Vermont	\$ 3,080	42	West Virginia	\$ 2,413
18	Colorado	\$ 3,073	43	Oklahoma	\$ 2,391
19	Wyoming	\$ 3,046	44	South Carolina	\$ 2,379
<b>20</b>	<b>OHIO</b>	<b>\$ 3,016</b>	45	Montana	\$ 2,363
21	Pennsylvania	\$ 2,979	46	South Dakota	\$ 2,299
22	Virginia	\$ 2,978	47	Arkansas	\$ 2,230
23	Nevada	\$ 2,915	48	Mississippi	\$ 2,214
24	Nebraska	\$ 2,906	49	Tennessee	\$ 2,185
25	Georgia	\$ 2,841	50	Alabama	\$ 2,117

**U.S. Average = \$ 3,095**

Source: Federation of Tax Administrators and U.S. Census Bureau. For state governments, figures generally represent a fiscal year ended June 30, 2000 and for local governments a calendar year ending December 31, 1999.

As the above table illustrates, the range of per capita taxes is considerable. Connecticut is the highest at \$4,595 and Alabama is lowest at \$2,117. This means that, on a “per person” basis, Ohioans paid \$1,579 less than residents of Connecticut, but \$899 more than residents of Alabama. Ohio’s per capita taxes of \$3,016 were slightly below the U.S. average of \$3,095.

The table below was prepared in a similar way, but it compares tax levels in each state with the state’s personal income. The Ohio ranking is 20<sup>th</sup> by this measure also.

### **Ohio Ranks 20<sup>th</sup> in State and Local Taxes As A Percentage of Income**

<u>Rank</u>	<u>State</u>	<u>Taxes As Percentage of Income</u>	<u>Rank</u>	<u>State</u>	<u>Taxes As Percentage of Income</u>
1	New York	14.1%	26	Massachusetts	11.0%
2	Maine	13.9%	27	Maryland	11.0%
3	Alaska	13.2%	28	Louisiana	11.0%
4	Wisconsin	12.9%	29	Nebraska	10.9%
5	New Mexico	12.7%	30	Georgia	10.9%
6	Hawaii	12.6%	31	Kansas	10.9%
7	Minnesota	12.4%	32	Washington	10.8%
8	Vermont	12.2%	33	Illinois	10.7%
9	California	12.0%	34	Oklahoma	10.7%
10	Connecticut	12.0%	35	North Carolina	10.7%
11	Utah	11.9%	36	Pennsylvania	10.7%
12	North Dakota	11.9%	37	Arkansas	10.7%
13	Rhode Island	11.8%	38	Indiana	10.6%
14	Wyoming	11.8%	39	Oregon	10.6%
15	West Virginia	11.6%	40	South Carolina	10.5%
16	Delaware	11.6%	41	Nevada	10.5%
17	Idaho	11.5%	42	Colorado	10.4%
18	Michigan	11.4%	43	Virginia	10.3%
19	New Jersey	11.3%	44	Florida	10.0%
<b>20</b>	<b>OHIO</b>	<b>11.3%</b>	45	Missouri	9.9%
21	Arizona	11.2%	46	Texas	9.7%
22	Kentucky	11.2%	47	South Dakota	9.5%
23	Iowa	11.1%	48	Alabama	9.4%
24	Mississippi	11.1%	49	Tennessee	8.9%
25	Montana	11.1%	50	New Hampshire	8.8%

**U.S. Average = 11.2%**

Source: same as previous table

As with the first comparison, this one shows a considerable range among the states. New York ranks highest, with taxes amounting to 14.1% of that state’s personal income. New Hampshire ranks lowest, with taxes amounting to just 8.8% of income. State and local taxes amount to 11.3% of personal income in Ohio, roughly the middle of the pack.

**How Do the Tax Foundation Rankings Compare To All The Others?**

All four of the authoritative sources cited in this report have published tax rankings that are similar or identical to those shown in the two tables on the previous pages. In contrast, the rankings produced by the Tax Foundation display widely different results, particularly for Ohio. For comparison purposes, here is Ohio’s rank for both measures in the latest figures reported by all five organizations.

**Ohio’s Tax Ranking (From Latest Published Report of Each Group)**

<u>Organization</u>	<u>Rank Per Capita</u>	<u>Rank As % of Income</u>
Federation of Tax Administrators (FTA)	20	20
Congressional Quarterly	20	20
Ohio Department of Taxation	20	20
Ohio Public Expenditure Council	20	22
Tax Foundation	11	3

All four of the authoritative organizations cited in this report rank Ohio 20<sup>th</sup> in per capita taxes. Three of them also rank the Buckeye State 20<sup>th</sup> in taxes as a percentage of income, while the other ranks Ohio 22<sup>nd</sup>.

Tax Foundation, in contrast, ranks Ohio taxes as 3<sup>rd</sup> highest in the nation, based on taxes compared to income. In per capita terms, their figures would place Ohio 11<sup>th</sup>, although that ranking does not actually appear in their reports, since their major focus is the percentage of income measure.

**Why Are the Tax Foundation Rankings So Different From All The Others?**

How can the Tax Foundation results be so completely different from all the others? Answering that question requires examining the methodology used to compute the figures. Both the figures and methodology are contained in an April 2004 “Special Report” available on the organization’s website, [www.taxfoundation.org](http://www.taxfoundation.org). The report is titled, “America Celebrates Tax Freedom Day.”

### ***Tax Foundation “Adjusts” the Data***

Ultimately, however, a careful reading of the report and its methodology raises more questions than answers. Tax Foundation apparently starts with the same Census Bureau data that other organizations use, although their report never specifically acknowledges it. The key difference between their conclusions and those of others is that Tax Foundation makes a series of adjustments or modifications to the Census data before computing state rankings. None of the other organizations adjusts the figures.

There are at least four adjustments made by Tax Foundation to the Census Bureau data. The one that may be most important, however, is not mentioned in the sixteen-page report. Tax Foundation claims their figures and rankings represent calendar year 2004. In fact, Table 5 in the “Special Report” showing Ohio with the 3<sup>rd</sup> highest taxes in the nation has “Calendar Year 2004” as part of its title.

Because the report was published in April 2004, it is clear that estimates needed to be made for that year, since no actual data could possibly be available before the year was even half over. Even more importantly, the most current Census Bureau data available in April 2004 (and even as of this writing) is the same 2000 data that was used for the rankings by the other four organizations cited here.

It is obvious, then, that Tax Foundation must have made assumptions about how tax levels, and presumably tax laws and rates, *changed* in the fifty states and 80,000 local governments from 2000 to 2004. No mention is made of this in their report.

### ***Tax Foundation’s Explanation of Other Adjustments is cursory***

Some information is provided about the three other adjustments made to each state’s data before the Tax Foundation rankings are compiled, although even it is fairly sketchy. Those adjustments are part of what they refer to as an “incidence analysis” that attempts to determine how the burden of taxes collected in a state may ultimately be shifted to residents of other states.

The first adjustment Tax Foundation makes is for state severance taxes. Observing that Alaska levies significant taxes on oil extracted from the state, they suggest that these taxes are incorporated into the price of gasoline and therefore shifted to consumers in other states. Using this logic, Tax Foundation adjusts the figures for taxes as a percentage of income, reducing the Alaska amount and increasing other states’ amounts for the “exported” Alaska burden. The specific adjustments are not shown.

In a similar fashion, Tax Foundation makes a second adjustment for state taxes imposed on tourism. Here is a quote from their report: “States where tourism constitutes a disproportionately large fraction of economic activity are therefore exporters of tax burdens because they are collecting taxes from many out-of-state residents. Nevada, Florida, and Louisiana are the three biggest exporters, while Pennsylvania, Illinois, and Texas are the biggest importers.” (Pages 15-16 of “Special Report”).

The third adjustment made by Tax Foundation is for corporate income taxes. Clearly, this could be cause for a significant modification in the figures due to the amounts involved, but the report contains no data or useful information on the actual adjustments made.

### ***Tax Foundation Ranking Assumes Ohio “Imports” \$675 Million in Taxes***

Table 7 on Page 15 in the Tax Foundation report summarizes the dollar amounts subtracted or added to each state’s taxes for the net combined total of these three adjustments. Ohio is shown as “importing” over \$675 million in taxes from other states. This is obviously one explanation for the major difference in state tax rankings between all other researchers and Tax Foundation.

Like so much of the Tax Foundation report, the figures in the table raise more questions than answers. For example, the State of Florida, which might logically be expected to “export” a very large amount of taxes due to its huge tourism industry, is shown as a net “importer” of taxes. Hawaii, another state highly dependent on tourism, is also shown as a tax “importer.”

On the other hand, New York and New Jersey are shown as “exporting” large amounts of taxes to other states. Since New York is specifically mentioned in the report as one of the three states that imports the largest portion of other states’ severance taxes, it is difficult to understand how New York ends up as a net *exporter* of almost \$3 billion in taxes. Because the necessary details are absent, the reader is left wondering how all of these unexplained calculations can so significantly revise the state tax rankings.

### ***Does Ohio’s Sales Tax Increase Explain Its Tax Foundation Ranking?***

One additional question might be posed in trying to understand how Tax Foundation could show Ohio as the third highest taxing state in the nation. Ohio did increase its state sales tax rate from 5% to 6% in July 2003. Could that possibly explain how Ohio might have leaped ahead of so many states in the Tax Foundation rankings? A simple illustration can show this is not the case, even assuming other states were not also raising their taxes in the difficult budget environment of the past four years.

The per capita numbers will be used for this illustration only because they make for a simpler example. Looking back to the table on page 4 of this report showing Ohio ranks 20<sup>th</sup> in per capita taxes, it is possible to guess what Ohio’s rank might be with the higher sales tax incorporated into the figures by making some simplifying assumptions.

Based on Ohio’s actual FY 2000 sales tax collections of \$6,214 million from a 5% tax, each 1% in rate produces about \$1,243 million, or \$109 per capita for Ohio’s population of 11,353,000. Adding \$109 to Ohio’s taxes would have raised Ohio’s per capita total from \$3,016 to \$3,125. This would have caused Ohio to move up three notches in the rankings to 17<sup>th</sup>, displacing Vermont on the table. As this example illustrates, it would



take an enormous increase in Ohio's taxes to move from 20<sup>th</sup> place to 3<sup>rd</sup> place, an increase far beyond anything that happened in Ohio in the past four years.

Moreover, it is unrealistic to assume other states did not increase their taxes between 2000 and 2004. Much of this period represented an exceedingly difficult budget environment for nearly all states, filled with spending reductions, cutbacks, and tax increases to keep budgets in balance. In 2003 alone, forty states imposed net tax increases, according to the National Conference of State Legislatures. Without knowing how other states have changed their tax rates and tax levels, it is not possible to accurately determine how Ohio's changes may have affected our ranking.

### **What is the Contribution of *Local* Taxes to Ohio's State and Local Tax Ranking?**

As noted earlier, the 50-state tables shown in this report display state and local taxes combined, rather than separating state taxes from local taxes. Public finance experts generally agree that for most purposes this is the more useful comparison among states since it represents the more complete tax burden measure.

Different states have chosen through policy decisions over the years to assign varying funding responsibilities between the state and its local governments. For this reason, states with relatively low state taxes may have relatively high local taxes, as they have in effect pushed responsibility for public services such as education more to the local level. Conversely, states with high state taxes often have relatively low taxes levied by their schools, cities, and counties. Although measuring tax levels by the combined state and local amount addresses these varying shares of funding responsibility, it can be instructive to view the two levels separately. The tables below contain comparisons between Ohio and national averages for state taxes alone and for local taxes alone so that the contribution of local taxes to the overall rankings can be gauged.

Interestingly, Ohio's state-levied taxes (i.e., those enacted by the state legislature) amount to \$1,733 per capita and rank 34<sup>th</sup>, lower than all but 16 states. Conversely, Ohio's local taxes are \$1,283 per capita, 9<sup>th</sup> highest in the nation. (It might also be observed here that, under Ohio law, much of this local burden has been imposed directly by local voters rather than elected officials.) Combining these state and local burdens yields the figure of \$3,016 in per capita state and local taxes, and the ranking of 20<sup>th</sup>, explained earlier.

The figures measuring taxes against personal income show a similar pattern. Although Ohio's state and local combined taxes are 11.3% of income for a ranking of 20<sup>th</sup>, our state tax ranking is 37<sup>th</sup>, while our local tax ranking is 6<sup>th</sup>.

### Per Capita State and Local Taxes: Ohio, U.S. Average, Ohio Rank

	State	Local	State and Local Combined
Ohio	\$ 1,733	\$ 1,283	\$ 3,016
U.S. Average	\$ 1,922	\$ 1,173	\$ 3,095
Ohio Rank	34	9	20

### State and Local Taxes As A Percentage of Income: Ohio, U.S. Average, Ohio Rank

	State	Local	State and Local Combined
Ohio	6.5%	4.8%	11.3%
U.S. Average	7.0%	4.2%	11.2%
Ohio Rank	37	6	20

### Summary and Conclusion

Ohio's overall level of state and local taxes is fairly average when compared to all other states. Ohio's per capita taxes are \$3,016 compared to the U.S. average of \$3,095, and rank 20<sup>th</sup> among the fifty states. Expressed as a percentage of personal income, Ohio's taxes are 11.3% compared to the U.S. average of 11.2%, again ranking 20<sup>th</sup>. These results are based on data from the U.S. Census Bureau, generally representing FY 2000, and the conclusions of four respected organizations, two national and two in Ohio.

A recent report by the Washington D.C.-based Tax Foundation concluding that Ohio has the 3<sup>rd</sup> highest taxes in the nation distorts the data by applying a series of at least four adjustments, none of which is fully or adequately explained in their report. As a simple example of this distortion, it can be observed that Tax Foundation adds \$675 million of taxes collected by other states to Ohio's tax collection totals before the state rankings are compiled. In contrast, their report subtracts over \$3 billion from New York's tax collections before computing that state's tax ranking.

The Tax Foundation report and conclusions fail the most basic test of sound research. Their results are neither transparent nor replicable. It is not possible to determine how they computed their figures and it is not possible to duplicate their methods. Until a far more convincing and detailed methodology is presented and published by Tax Foundation, the results found by the four organizations cited here should continue to be the standard for comparative state tax rankings. And Ohio should continue to be regarded as an average state in the comparative rankings.