Future State Business Tax Reforms: Perspectives from the Business, Government, and Academic Communities

Lessons Learned - Ohio

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Lessons Learned - Agenda

- Background on Ohio and Its Tax Reform Efforts
- Overview of the Reform and the Commercial Activity Tax (the “CAT”)
- Why It Works and Lessons Learned

Background on Ohio

and Its

Tax Reform Efforts

Ohio . . . an Economic Powerhouse

	1964
Personal Income Tax Rate (HMR)	Zero
Corporate Income Tax Rate (HMR)	Zero
Sales Tax Rate (State Only)	3%
Tangible Personal Property Listing %	50%-70%
Number of Cities with an Income Tax	~130

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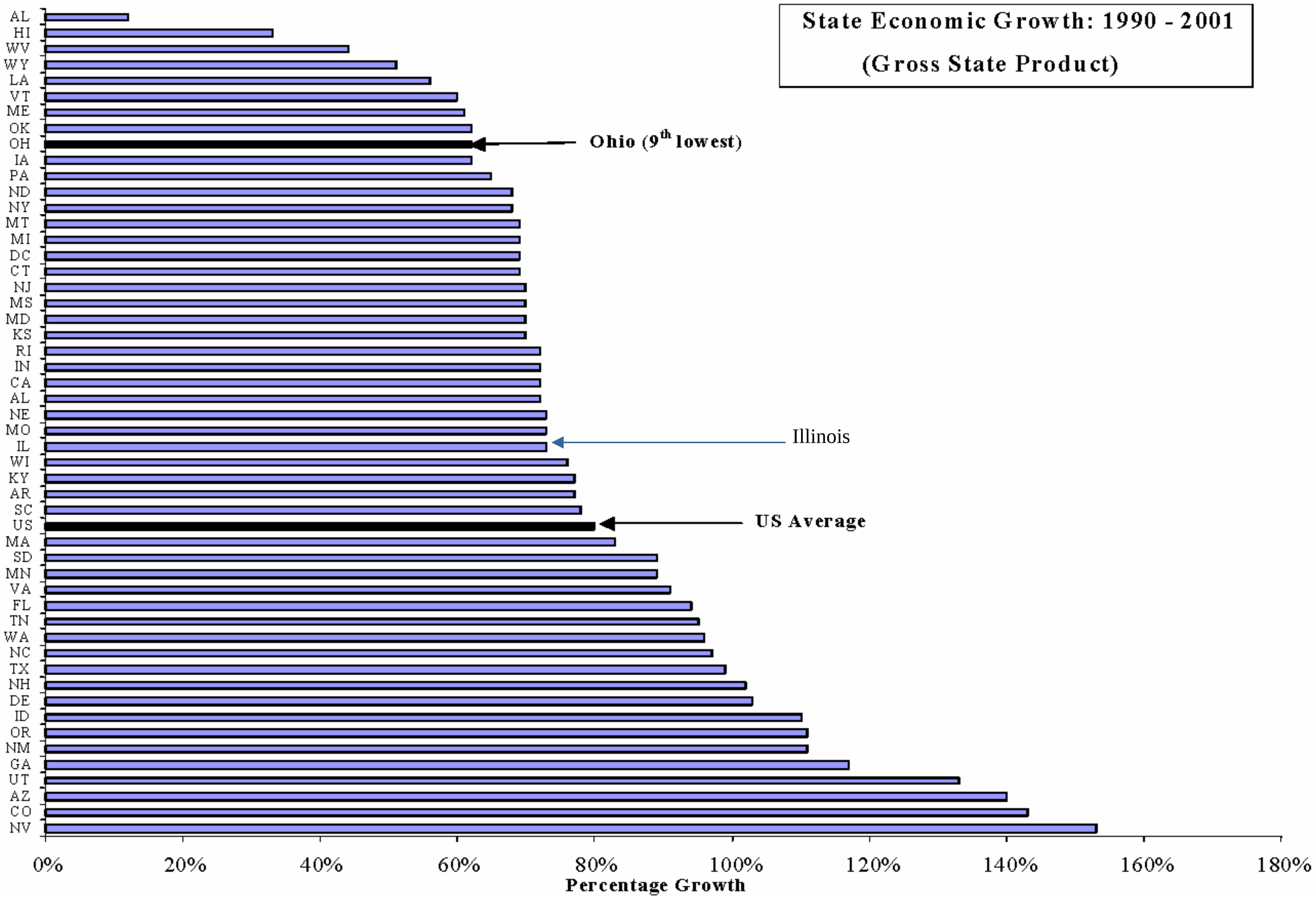
Ohio's Declining Economic Performance

- From 1990 – 2001, Ohio ranked 9th lowest among states in the rate of growth of the overall economy
  - 20% below average for all states
- Growth in manufacturing (nearly 25% of Ohio's economy) was 40% U.S. average
- Job growth was 20% below national average



Source: Ohio Business Roundtable

Ohio . . . 40 Years of Tax Changes

	1964	2004
Personal Income Tax Rate (HMR)	Zero	7.5%
Corporate Income Tax Rate (HMR)	Zero	8.9%
Sales Tax Rate (State Only)	3%	6%
Tangible Personal Property Listing %	50%-70%	25%
Number of Cities with an Income Tax	~130	~540

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Ohio Business Roundtable

- CEO-driven business organization, representing Ohio's largest companies
  - Tax reform was the #1 issue for 80 of Ohio's largest companies

- Project team included tax professionals from around Ohio and from member companies

- Developed economic models to evaluate tax changes and impact on the economy
  - Retained: Ernst & Young, LLP

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Overview of the Reform

and the

Commercial Activity Tax

Overview of the Reform – Beg. 7/1/05

- Commercial Activity Tax Phased-In
  - Over 5 Years
- Tangible Personal Property Tax Elimination
  - Over 3 Years
- Corporation Franchise Tax Elimination
  - Over 5 Years
- 21% Personal Income Tax Cut
  - Over 5 Years

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40 Years Later . . . Plus 6

	1964	2004	2010
Personal Income Tax Rate (HMR)	Zero	7.5%	5.925%
Corporate Income Tax Rate (HMR)	Zero	8.5%	Zero
Sales Tax Rate (State Only)	3%	6%	5.5%
Tangible Personal Property Listing %	50%-70%	25%	Zero
Number of Cities with an Income Tax	~130	~540	~540

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Business View

- Many businesses supported Governor Taft's tax reform package
  - Generally larger businesses with large Ohio base of operations or corporate headquarters
  - Generally businesses paying lots of corporation franchise tax and tangible personal property tax

Business View

- Many businesses did not support the Governor's tax reform package
  - Some very large businesses with non-Ohio headquarters
    - Less CFT and TPP tax
    - Little PIT benefit
  - High-volume, low margin businesses
    - Market driven companies

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CAT Calculation

"Taxable Gross Receipts"

<u>X   0.0026</u>

Full CAT

<u>X Phase-in Percentage</u>

Phased-In CAT

<u>- CAT Credits</u>

CAT Due*

* Must add $150 Minimum Tax.

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Entities Subject to CAT

- Individuals
- Corporations
- S Corporations
- QSSS
- Partnerships
- LLCs and LLPs
- Firms
- Companies
- Estates
- Trusts
- Disregarded Entities
- Joint ventures
- Associations
- Societies
- Clubs

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Some Entities Not Subject to CAT

- Any person with $150,000 or less of taxable gross receipts.
- Certain public utilities
- Banks, other financial institutions, and their affiliates
- Domestic or foreign insurance companies.
- Nonprofit organizations

Some Exclusions from Gross Receipts

- Interest, except on credit sales.
- Dividends.
- Wages.
- Distributive shares of PTE income.
- Amounts received from sale, exchange or disposition of section 1221 or 1231 property.

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Why It Works

and the

Lessons Learned

Why It Works

- Ohio did “Economic Reform”
  - Not “Tax Reform”
- Ohio’s Reform Resulted in a Tax Cut for most businesses and Ohioans

Ohio – FY 2010

- Gross state product will increase by $5.6 billion.
- Personal income will increase by $3.6 billion.
- 78,500 new jobs will be created.
- An additional $6.3 billion in real fixed capital investment will be injected into the economy.
- Plus, $401 million in new state tax revenue will be generated.
- Per ODT, projected net tax reduction of $3.8 billion of tax.

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Why It Works

- CAT has Serious Issues, But Offset in Ohio by:
  - Elimination of Tangible Property Tax and the Corporation Franchise Tax
    - Business Tax reduction of $1.5 billion in 2010 (net of CAT)
  - Very Low Rate
  - Significant Personal Income Tax Cuts
    - $2.3 billion less tax in 2010

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Reform – Lessons Learned

- Business buy-in and data is crucial to true reform.
  - Format (i.e., taxing investment v. taxing consumption).
  - Benefits (i.e., net cuts or revenue neutrality).
- Economic reform, not tax reform.
- Focus on quality principles – system should be competitive, simple, stable, fair and neutral.
  - Everyone can agree on these.
- Don’t try to make everyone happy—but make a lot of folks happy!

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