

# BACKGROUND PAPER

October 2008, Number 58

## 2009 State Business Tax Climate Index

**By**  
Joshua Barro  
Staff Economist  
Tax Foundation

### Introduction

The Tax Foundation presents the 2009 version of the State Business Tax Climate Index (SBTCI) as a tool for lawmakers, the media and individuals alike to gauge how their states' tax systems compare. Policymakers can use the SBTCI to pinpoint changes to their tax systems that will explicitly improve their states' standing in relation to competing states.

American companies often function at a competitive disadvantage in the global economy. They pay one of the highest corporate tax rates of any of the industrialized countries. The top federal rate on corporate income is 35 percent, and states with punitive tax systems cause companies to be even less competitive globally.

The modern market is characterized by mobile capital and labor. Therefore, companies will locate where they have the greatest competitive advantage. States with the best tax systems will be the most competitive in attracting new businesses and most effective at generating economic and employment growth.

Although the market is now global, the Department of Labor reports that most mass job relocations are from one U.S. state to another rather than to an overseas location.<sup>1</sup> Certainly job creation is rapid overseas, as previously underdeveloped nations enter the

world economy. So state lawmakers are right to be concerned about how their states rank in the global competition for jobs and capital, but they need to be more concerned with companies moving from Ithaca, NY, to Indianapolis, IN, to rather than from Ithaca to India. This means that state lawmakers must be aware of how their states' business climates match up to their immediate neighbors and to other states within their regions.

Anecdotes about the impact of state tax systems on business investment are plentiful. In Illinois, hundreds of millions of dollars of capital expenditures were delayed when Governor Blagojevich proposed a hefty gross receipts tax. Only when the legislature resoundingly defeated the bill did the investment resume. In 2005, Intel decided to build a multi-billion dollar chip-making facility in Arizona due to its favorable corporate income tax system. California struggles to retain businesses within its borders because Nevada provides a low-tax alternative. Anecdotes such as these reinforce what we know from economic theory: taxes matter to businesses, and those places with the most competitive tax systems will reap the benefits of business-friendly tax climates.

State lawmakers are always mindful of their states' business tax climates but they are often tempted to lure business with lucrative tax incentives and subsidies instead of broad-

<sup>1</sup> U.S. Department of Labor, "Extended Mass Layoffs in the First Quarter of 2007," August 9, 2007, located at <http://www.bls.gov/news.release/mslo.nr0.htm>. In the press release, DOL reported that: "In the 61 actions where employers were able to provide more complete separations information, 84 percent of relocations (51 out of 61) occurred among establishments within the same company. In 64 percent of these relocations, the work activities were reassigned to places elsewhere in the U.S. Thirty-six percent of the movement-of-work relocations involved out-of-country moves (22 out of 50)." (internal references omitted).

based tax reform. This can be a dangerous proposition, as a case in Florida illustrates. In July of 2004 Florida lawmakers cried foul because a major credit card company announced it would close its Tampa call center, lay off 1,110 workers, and outsource those jobs to another company. The reason for the lawmakers' ire was that the company had been lured to Florida with a generous tax incentive package and had enjoyed nearly \$3 million worth of tax breaks during the previous nine years.<sup>2</sup> A recent *USA Today* article chronicled similar problems other states are having with companies who receive generous tax incentives.<sup>3</sup>

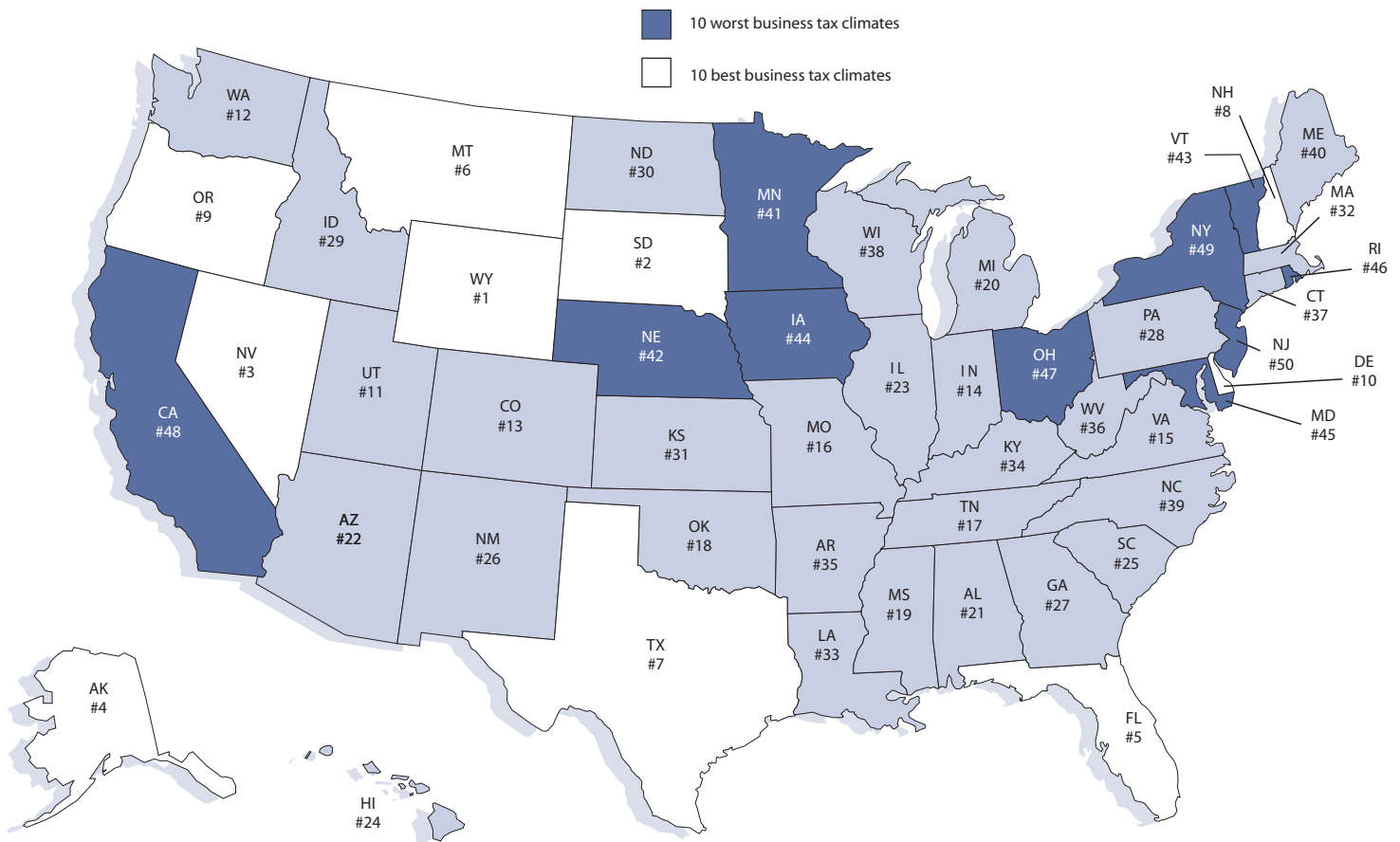
Lawmakers create these deals under the banner of job creation and economic development, but the truth is that if a state needs to offer such packages, it is most likely covering for a woeful business tax climate. A far more effective approach is to systematically improve the business tax climate for the long term so as to improve the

state's competitiveness. When assessing which changes to make, lawmakers need to remember these two rules:

1. Taxes matter to business. Business taxes affect business decisions, job creation and retention, plant location, competitiveness, the transparency of the tax system, and the long-term health of a state's economy. Most importantly, taxes diminish profits. If taxes take a larger portion of profits, that cost is passed along to either consumers (through higher prices), workers (through lower wages or fewer jobs), or shareholders (through lower dividends or share value). Thus a state with lower tax costs will be more attractive to business investment, and more likely to experience economic growth.
2. States do not enact tax changes (increases or cuts) in a vacuum. Every tax law will in some way change a state's competitive position relative to its immediate neighbors, its geo-

**Figure 1**

*State Business Tax Climate Index, Fiscal Year 2009*



<sup>2</sup> Dave Wasson, "Florida Lawmakers Slam Capital One's Layoff After Years of Tax Breaks," *Tax Analysts*, July 27, 2004.

<sup>3</sup> Dennis Cauchon, "Business Incentives Lose Luster for States," *USA Today* (8/22/2007).

graphic region, and even globally. Ultimately it will affect the state's national standing as a place to live and to do business. Entrepreneur-

ial states can take advantage of the tax increases of their neighbors to lure businesses out of high-tax states.

**Table 1**  
*State Business Tax Climate Index, 2006 – 2009*

State	FY 2009 State Business Tax Climate Index		FY 2008 State Business Tax Climate Index		Change from 2008 to 2009		FY 2007 State Business Tax Climate Index		FY 2006 State Business Tax Climate Index	
	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank
U.S.	5.00	–	5.00	–	5.00	–	5.00	–	5.00	–
Alabama	5.33	21	5.38	20	–0.05	–1	5.46	19	5.61	15
Alaska	7.33	4	7.28	4	0.05	0	7.30	3	7.37	3
Arizona	5.27	22	5.30	21	–0.03	–1	5.22	27	5.24	28
Arkansas	4.90	35	4.90	37	0.00	2	4.84	37	4.81	37
California	4.15	48	3.99	48	0.16	0	4.03	47	4.08	46
Colorado	5.93	13	5.94	12	–0.01	–1	5.86	11	5.88	12
Connecticut	4.84	37	4.95	36	–0.11	–1	4.88	36	4.71	39
Delaware	6.02	10	6.05	10	–0.03	0	6.12	8	6.15	8
Florida	6.93	5	6.93	5	0.00	0	6.81	5	6.86	5
Georgia	5.19	27	5.21	26	–0.02	–1	5.30	22	5.31	23
Hawaii	5.24	24	5.26	22	–0.02	–2	5.24	25	5.33	22
Idaho	5.12	29	5.19	29	–0.07	0	5.11	30	5.15	30
Illinois	5.27	23	5.23	23	0.04	0	5.28	23	5.27	24
Indiana	5.91	14	5.99	11	–0.08	–3	5.84	13	5.92	11
Iowa	4.37	44	4.42	45	–0.05	1	4.57	43	4.64	43
Kansas	5.10	31	5.03	33	0.07	2	5.07	31	5.02	33
Kentucky	4.98	34	4.97	34	0.01	0	4.76	39	4.72	38
Louisiana	5.01	33	4.95	35	0.06	2	5.04	33	5.08	32
Maine	4.71	40	4.68	40	0.03	0	4.73	40	4.65	42
Maryland	4.33	45	5.23	24	–0.90	–21	5.14	29	5.24	27
Massachusetts	5.03	32	5.05	31	–0.02	–1	4.98	34	4.97	34
Michigan	5.34	20	5.22	25	0.12	5	5.20	28	5.26	25
Minnesota	4.64	41	4.68	41	–0.04	0	4.64	41	4.67	41
Mississippi	5.34	19	5.39	19	–0.04	0	5.50	17	5.50	18
Missouri	5.60	16	5.61	15	–0.01	–1	5.46	18	5.48	19
Montana	6.29	6	6.32	6	–0.03	0	6.17	7	6.14	9
Nebraska	4.58	42	4.53	43	0.06	1	4.40	45	4.47	45
Nevada	7.38	3	7.38	3	–0.01	0	7.26	4	7.26	4
New Hampshire	6.17	8	6.27	7	–0.10	–1	6.02	10	6.27	7
New Jersey	3.92	50	3.84	50	0.09	0	4.08	46	3.76	48
New Mexico	5.19	26	5.19	28	0.00	2	5.26	24	5.26	26
New York	4.02	49	4.06	47	–0.03	–2	3.97	48	3.59	49
North Carolina	4.76	39	4.64	42	0.12	3	4.60	42	4.56	44
North Dakota	5.10	30	5.03	32	0.07	2	5.06	32	5.12	31
Ohio	4.16	47	4.11	46	0.05	–1	3.95	49	3.93	47
Oklahoma	5.44	18	5.41	18	0.02	0	5.39	20	5.36	20
Oregon	6.06	9	6.06	9	0.01	0	6.09	9	6.09	10
Pennsylvania	5.17	28	5.18	30	–0.01	2	5.39	21	5.35	21
Rhode Island	4.20	46	3.98	49	0.23	3	3.72	50	3.57	50
South Carolina	5.24	25	5.20	27	0.04	2	5.23	26	5.23	29
South Dakota	7.51	2	7.51	2	0.00	0	7.48	2	7.46	2
Tennessee	5.47	17	5.49	17	–0.02	0	5.50	16	5.50	17
Texas	6.28	7	6.21	8	0.08	1	6.47	6	6.43	6
Utah	5.98	11	5.53	16	0.45	5	5.67	15	5.74	14
Vermont	4.55	43	4.44	44	0.10	1	4.55	44	4.70	40
Virginia	5.73	15	5.78	14	–0.05	–1	5.70	14	5.59	16
Washington	5.94	12	5.91	13	0.03	1	5.85	12	5.85	13
West Virginia	4.88	36	4.84	38	0.04	2	4.95	35	4.94	35
Wisconsin	4.79	38	4.76	39	0.03	1	4.82	38	4.81	36
Wyoming	7.53	1	7.64	1	–0.11	0	7.70	1	7.68	1
D.C.	4.55	–	4.49	–	0.06	–	4.40	–	4.39	–

**Note:** The higher the score, the more favorable a state's tax system is for business. All scores are for fiscal years.

**Source:** Tax Foundation

Clearly, there are many non-tax factors that affect a state's overall business climate: its proximity to raw materials or transportation centers, its regulatory or legal structures, the quality of its education system and the skill of its workforce, not to mention the intangible perception of a state's "quality of life."<sup>4</sup> The 2009 SBTICI does not measure the impact of these important features of a state's overall business climate. Rather, the SBTICI merely seeks to measure the tax component of each state's business climate.

Some of the non-tax factors of a state's business climate are outside of the control of elected officials. Montana lawmakers cannot change the fact that Montana's businesses have no immediate access to deepwater ports. Lawmakers do, however, have direct control over how friendly their tax systems are to business. Furthermore, unlike changes to a state's health care, transportation or education system—which can take decades to implement—changes to the tax code bring almost instantaneous benefits to a state's business climate.

The ideal tax system—whether at the local, state or federal level—is simple, transparent, stable, neutral to business activity, and pro-growth. In such an ideal system, individuals and businesses would spend a minimum amount of resources to comply with the tax system, understand the true cost of the tax system, base their economic decisions solely on the merits of the transactions, without regard to tax implications, and not have the tax system impede their growth and prosperity.

In reality, tax-induced economic distortions are a fact of life, and a more realistic goal is to maximize the occasions when businesses and individuals are guided by business principles, and minimize those cases where economic decisions are micromanaged or even dictated by a tax system. Therefore, the most competitive tax systems, and the ones that score best in the SBTICI, are those that create the fewest economic distortions by enforcing the most simple, pro-growth tax systems characterized by broad bases and low rates.

The SBTICI does not measure business tax burdens. While it is unquestionably important how much revenue states collect in business taxes,

the manner in which they extract tax revenue is also important. In other words, quite apart from whether a state's total business tax burden is higher than in other states, it can enact (and many states do) a set of business tax laws that cause great damage to the economy. The SBTICI does not allow states with poor business tax regimes to hide behind low business tax burdens.

Good state tax systems levy low, flat rates on the broadest bases possible, and they treat all taxpayers the same. Variation in the tax treatment of different industries favors one economic activity or decision over another. The more riddled a tax system is with politically motivated preferences the less likely it is that business decisions will be made in response to market forces. The SBTICI rewards those states that apply these principles in five important areas of taxation: major business taxes, individual income taxes, sales taxes, unemployment insurance taxes and property taxes.

Tax competition is an unpleasant reality for state revenue and budget officials, but it is an effective restraint on state and local taxes. It also helps to more efficiently allocate resources because businesses can locate in the states where they receive the services they need at the lowest cost. When a state imposes higher taxes than a neighboring state, businesses will cross the border to some extent. Therefore states with more competitive tax systems score well in the SBTICI because they are best suited to generate economic growth.

Ranking the competitiveness of 50 very different tax systems presents many challenges, especially when a state dispenses with a major tax entirely. Should Colorado's tax system, which includes three relatively neutral taxes on general sales, individual income and corporate income, be considered more or less competitive than Alaska's tax system, which includes a particularly burdensome corporate income tax but no tax on individual income or general statewide sales?

The 2009 SBTICI deals with such questions by comparing the states on five separate aspects of their tax systems and then adding the results up to a final, overall ranking. This approach has the advantage of rewarding states on particularly strong aspects of their tax systems (or penalizing them on particularly weak aspects) while also measuring the general competitiveness of their

<sup>4</sup> A trend in tax literature throughout the 1990s has been the increasing use of indexes to measure a state's general business climate. These include the Center for Policy and Legal Studies' "Economic Freedom in America's 50 States: A 1999 Analysis" and the Beacon Hill Institute's "State Competitiveness Report 2001." Such indexes even exist on the international level, including the Heritage Foundation and *Wall Street Journal's* "2004 Index of Economic Freedom." Plaut and Pluta (1983) examined the use of business climate indexes as explanatory variables for business location movements. They found that such general indexes do have a significant explanatory power, helping to explain, for example, why businesses have moved from the Northeast and Midwest towards the South and Southwest. In turn, they also found that high taxes have a negative effect on employment growth.



overall tax systems. The result is a score that can be compared to other states' scores. Ultimately, both Alaska and Colorado score well.

This edition is the 2009 SBTCI and represents the tax climate of each state as of July 1, 2008, the first day of the standard 2009 fiscal year.

## The Best and Worst Business Tax Climates

The ten best states in the Tax Foundation's 2009 State Business Tax Climate Index are as follows:

- |                 |                  |
|-----------------|------------------|
| 1. Wyoming      | 6. Montana       |
| 2. South Dakota | 7. Texas         |
| 3. Nevada       | 8. New Hampshire |
| 4. Alaska       | 9. Oregon        |
| 5. Florida      | 10. Delaware     |

It is obvious that the absence of a major tax is a dominant factor in vaulting these ten states to the top of the rankings. Property taxes and unemployment insurance taxes are levied in every state, but there are several states that do without one or more of the major taxes: the corporate tax, the individual income tax, or the sales tax. Wyoming, Nevada and South Dakota have no corporate or individual income tax; Alaska has no individual income or state-level sales tax; Florida and Texas have no individual income tax; and New Hampshire, Delaware, Oregon and Montana have no sales tax.

The lesson is simple; a state that raises sufficient revenue without one of the major taxes will, all things being equal, out-compete those states that levy every tax in the state tax collector's arsenal.

The ten worst states in the SBTCI are as follows:

- |               |                  |
|---------------|------------------|
| 41. Minnesota | 46. Rhode Island |
| 42. Nebraska  | 47. Ohio         |
| 43. Vermont   | 48. California   |
| 44. Iowa      | 49. New York     |
| 45. Maryland  | 50. New Jersey   |

New Jersey scores at the bottom by having the third worst individual income tax, tenth worst sales tax, and worst property tax. Rhode Island has the worst unemployment tax system, the fifth worst property tax system, and the ninth worst

individual income tax system.<sup>5</sup> Maryland managed a remarkable drop—from 24<sup>th</sup> in last year's index to 45<sup>th</sup> in this year's—by raising its individual income tax, corporate income tax, sales tax and cigarette tax all in the same year. Maryland added four new brackets to the individual income tax, increasing the top rate by 1.5%, adding new complexity, and introducing a big marriage penalty. In fact, we now rate Maryland's as by far the worst individual income tax in America, displacing California for that dubious distinction. The remaining states in the bottom ten suffer from the same afflictions that plague these three states: complex, non-neutral taxes with comparatively high rates.

A detailed description of each component index, each sub-index, and their various components is presented later in the paper, and those states that score especially well or poorly on each component are discussed to provide guidance on the changes that each state might well contemplate.

## A Review of the Economic Literature

Economists have not always agreed on how individuals and businesses react to taxes. As early as 1956, Charles Tiebout postulated that if citizens were faced with an array of communities that offered different types or levels of public goods and services at different costs or tax levels, then all citizens would choose the community that best satisfied their particular demands, revealing their preferences by "voting with their feet." Tiebout's article is the seminal work on the topic of taxation affecting the location decisions of taxpayers.

Tiebout also suggested that citizens with high demands for public goods would concentrate themselves in communities with high levels of public services and high taxes while those with low demands would choose communities with low levels of public services and low taxes. Competition among jurisdictions results in a variety of communities, each with residents that all value public services similarly.

### MARYLAND

Maryland ranks 45<sup>th</sup> overall, a drastic drop from its 24<sup>th</sup> rank last year. Maryland lawmakers achieved this remarkable feat by raising most of the state's major taxes for FY 2009. They raised the corporate income tax rate to 8.25% from 7%, the sales tax rate to 6% from 5%, and the cigarette excise tax to \$2.00 from \$1.00 per pack. They also created four new income tax brackets, raising taxes on filers earning more than \$150,000 per year. Maryland's top personal income tax rate is now 6.25% (up from 4.75%); that's on top of a weighted average local option rate of 2.98%. Maryland now has by far the worst personal income tax in the country, with a significantly lower score than second-place California.

<sup>5</sup> Rhode Island lawmakers passed an optional flat tax on individual income starting with an 8 percent rate for 2006 (scheduled to decrease to 5.5 percent by 2011). Filers can calculate their liabilities under both laws—the old rates and brackets and the new flat tax—and pay the lower amount. The SBTCI scores Rhode Island's income tax based on the old, graduated system, except that the sub-index score for the top tax rate is based on the flat system, as many high-income filers who would have been subject to the 9.9% top graduated rate are expected to file under the flat system. Therefore, Rhode Island's score improves each year as the flat rate falls; Rhode Island was 48th best on the 2007 income tax index, but moves up to 42nd best this year.

However, businesses sort out the costs and benefits of taxes differently from individuals. To businesses, which can be more mobile and must earn profits to justify their existence, taxes reduce profitability. Theoretically, then, businesses could be expected to be more responsive than individuals to the lure of low-tax jurisdictions.

The economic literature over the past 50 years has slowly cohered around this hypothesis. Ladd (1998) summarizes the post-World War II empirical tax research literature in an excellent survey article, breaking it down into three distinct periods of differing ideas about taxation: (1) taxes do not change behavior; (2) taxes may or may not change business behavior depending on the circumstances; (3) taxes definitely change behavior.

Period one, with the exception of Tiebout, included the 1950s, '60s and '70s and is summarized succinctly in three survey articles: Due (1961), Oakland (1978) and Wasylenko (1981). Due's was a polemic against tax giveaways to businesses, and his simple analysis techniques consisted of basic correlations, interview studies and the examination of taxes relative to other costs. He found no evidence to support the notion that taxes influence business location.

Oakland was skeptical of the assertion that tax differentials at the local level had no influence at all. However, because econometric analysis was relatively unsophisticated at the time, he found no significant articles to support his intuition. Wasylenko's survey of the literature found some of the first evidence indicating that taxes do influence business location decisions. However, the statistical significance was lower than that of other factors such as labor supply and agglomeration economies. Therefore, he dismissed taxes as a secondary factor at most.

Period two was a brief transition during the early- to mid-1980s. This was a time of great ferment in tax policy as Congress passed major tax bills, including the so-called Reagan tax cut in 1981 and a dramatic reform of the tax code in 1986. Articles revealing the economic significance of tax policy proliferated and became more sophisticated. For example, Wasylenko and McGuire (1985) extended the traditional business location literature to non-manufacturing sectors and found, "Higher wages, utility prices, personal income tax rates, and an increase in the overall level of taxation discourage employment growth in several industries." However, Newman and Sullivan (1988) still found a mixed bag in "their observation that significant tax effects [only]

emerged when models were carefully specified." (Ladd, p. 89).

Ladd was writing in 1998, so her "period three" started in the late 1980s and continued up to 1998 when the quantity and quality of articles increased significantly. Articles that fit into period three begin to surface as early as 1985, as Helms (1985) and Bartik (1985) put forth forceful arguments based on empirical research that taxes guide business decisions. Helms concluded that a state's ability to attract, retain, and encourage business activity is significantly affected by its pattern of taxation. Furthermore, tax increases significantly retard economic growth when the revenue is used to fund transfer payments. Bartik found that the conventional view, as he describes it, that state and local taxes have little effect on business is false.

Papke and Papke (1986) found that tax differentials between locations may be an important business location factor, finding that consistently high business taxes can represent a hindrance to the location of industry. Interestingly, they use the same type of after-tax model used by Tannenwald (1996) who reaches a different conclusion.

Bartik (1989) provides strong evidence that taxes negatively impact business start-ups. He finds specifically that property taxes, because they are paid regardless of profit, have the strongest negative effect on business. Bartik's econometric model also predicts that tax elasticities of  $-0.1$  to  $-0.5$  imply that a ten percent cut in tax rates will increase business activity by 1 to 5 percent. Bartik's findings, as well as those of Mark, McGuire and Papke (2000), about property taxes buttress the argument, in addition to ample anecdotal evidence of the importance of property taxes, for inclusion of a property index devoted to property-type taxes in the SBTCL.

By the early 1990s, the literature expanded enough so that Bartik (1991) found 57 studies on which to base his literature survey. Ladd succinctly summarizes Bartik's findings:

The large number of studies permitted Bartik to take a different approach from the other authors. Instead of dwelling on the results and limitations of each individual study, he looked at them in the aggregate and in groups. Although he acknowledged potential criticisms of individual studies, he convincingly argued that some systematic flaw would have to cut across all studies for the consensus results to be invalid. In striking

contrast to previous reviewers, he concluded that taxes have quite large and significant effects on business activity (p. 92).

Ladd's "period three" surely continues to this day. Agostini and Tulayasathien (2001) examined the effects of corporate income taxes on the location of foreign direct investment in U.S. states. They determined that for "foreign investors, the corporate tax rate is the most relevant tax in their investment decision." Therefore, they found that foreign direct investment was quite sensitive to states' corporate tax rates (p. 28).

Mark, McGuire and Papke (2000) find that taxes are a statistically significant factor in private-sector job growth. Specifically, they find that personal property taxes and sales taxes have economically large negative effects on the annual growth of private employment (Mark, et al. 2000).

Harden and Hoyt (2003) point to Phillips and Gross (1995) as another study contending that taxes impact state economic growth, and they assert that the consensus among recent literature is that state and local taxes negatively affect employment levels. Harden and Hoyt conclude that the corporate income tax has the most significant negative impact on the rate of growth in employment.

Gupta and Hofmann (2003) regressed capital expenditures against a variety of factors, including weights of apportionment formulas, the number of tax incentives and burden figures. Their model covered 14 years of data and determined that firms tend to locate property in states where they are subject to lower income tax burdens. Furthermore, Gupta and Hofmann suggest that throwback requirements are most influential on the location of capital investment, followed by apportionment weights and tax rates, and that investment-related incentives have the least impact.

Other economists have found that taxes on specific products can produce behavioral results similar to those that were found in these general studies. For example, Fleenor (1998) looked at the effect of excise tax differentials between states on cross-border shopping and the smuggling of cigarettes. Moody and Warcholik (2004) examined the cross-border effects of beer excises. Their results, supported by the literature in both cases, showed significant cross-border shopping and smuggling between low-tax states and high-tax states.

Fleenor found that shopping areas sprouted in counties of low-tax states that shared a border with a high-tax state, and that approximately 13.3 percent of the cigarettes consumed in the United States during FY 1997 were procured via some type of cross-border activity. Similarly, Moody and Warcholik found that in 2000, 19.9 million cases of beer, on net, moved from low- to high-tax states. This amounted to some \$40 million in sales and excise tax revenue lost in high-tax states.

Even though the general tide of the literature has progressed to the point where the consensus is that taxes are a substantial factor in the decision-making process for businesses, there remain some authors who are not convinced.

Based on a substantial review of the literature on business climates and taxes, Wasylenko (1997) concludes that taxes do not appear to have a substantial effect on economic activity among states. He does, however, cite a *State Policy Report* article that asserts the opposite: that as long as the tax elasticity is negative and significantly different from zero, high-tax states will lose more economic activity than average or low-tax states. Indeed, *State Policy Report* continues, the highest-tax states, such as Minnesota, Wisconsin and New York, have acknowledged that high taxes may be responsible for the low rates of job creation in those states.<sup>6</sup>

Wasylenko's rejoinder is that policymakers routinely overestimate the degree to which tax policy affects business location decisions, and that as a result of this misperception, they respond readily to public pressure for jobs and economic growth by proposing lower taxes. According to Wasylenko, other legislative actions are likely to accomplish more positive economic results because in reality, taxes do not drive economic growth. He asserts that lawmakers need better advice than just "Lower your taxes," but there is no coherent message advocating a different course of action.

However, there is ample evidence that states certainly still compete for businesses using their

## FLORIDA

Over the year, Florida has had one of the most active taxation debates in the country. Much of the debate centered around a proposed constitutional amendment (Amendment 5), which would have eliminated certain school property taxes in favor of unspecified revenue-raising changes to the sales tax. These would have potentially included a broadening of the sales tax base and a rise in the rate from 6% to 7%. Ultimately, Amendment 5 was removed from the ballot by the courts, and Florida is unlikely to see major tax reform this year. Whatever Amendment 5's merits, that is no cause for sadness in Florida—the state ranks fifth overall in our index (unchanged from last year) and particularly benefits from its lack of a personal income tax. It's also one of just four states to rank in the top half on all five tax-specific indices. Even Florida's much-maligned property tax system ranks fairly well, scoring 19<sup>th</sup> out of 50 states. Of course, improvements can be made to any state's tax code, and expanding the sales tax base would likely be a good reform; but Florida is in a better position than most states to be content with the tax code it has.



tax systems. A recent example is that of Intel, an international firm that was enticed to build a plant in Arizona. From the *San Jose Mercury News*:

Intel will spend \$3 billion to build a next-generation chip factory in Chandler, Arizona. "California has been, in the last 10 to 15 years, pretty expensive," said Chuck Mulloy, an Intel spokesman.<sup>7</sup>

What in fact brought Intel to Arizona was not the type of special package or program targeted at just one firm. Arizona enacted a change in its apportionment formula from a 50 percent sales and 25 percent property and payroll apportionment formula to an 80 percent sales formula by 2009.

## Metrics to Measure the Impact of Tax Differentials

Some recent contributions to the literature on state taxation criticize business and tax climate studies in general. Authors of such studies contend that indexes like the State Business Tax Climate Index do not take into account those factors which directly impact a state's business climate. However, a careful examination of these criticisms reveals that the authors believe taxes are unimportant to businesses and therefore dismiss the studies as merely being designed to advocate low taxes.

Peter Fisher's *Grading Places: What Do the Business Climate Rankings Really Tell Us?*, published by the Economic Policy Institute, criticizes five indexes: The Small Business Survival Index published by the Small Business and Entrepreneurship Council, Beacon Hill's Competitiveness Reports, the Cato Institute's Fiscal Policy Report Card, the Economic Freedom Index by the Pacific Research Institute, and the 2003 edition of this study. Fisher concludes: "The underlying problem with the five indexes, of course, is twofold: none of them actually do a very good job of measuring what it is they claim to measure, and they do not, for the most part, set out to measure the right things to begin with." (Fisher 2005). Fisher's major argument is that if the indexes did what they purported to do, then all five of them would rank the states similarly.

Fisher's conclusion holds little weight because the five indexes serve such dissimilar purposes and each group has a different area of expertise. There is no reason to believe that the Tax Foundation's Index, which depends entirely on state tax laws, would rank the states in the same or similar order

as an index that includes crime rates, electricity costs and health care (Small Business and Entrepreneurship Council's Small Business Survival Index), or infant mortality rates and the percentage of adults in the workforce (Beacon Hill's State Competitiveness Report), or charter schools, tort reform and minimum wage laws (Pacific Research Institute's Economic Freedom Index).

The Tax Foundation's State Business Tax Climate Index is an indicator of which states' tax systems are the most hospitable to business and economic growth. The SBTICI does not attempt to measure economic opportunity or freedom, or even the broad business climate, but the narrower business tax climate. We do so not only because the Tax Foundation's expertise is in taxes, but because every component of the SBTICI is subject to immediate change by state lawmakers. It is by no means clear what the best course of action is for state lawmakers who want to thwart crime, for example, either in the short or long term, but they can change their tax codes now. The Tax Foundation believes business decisions are significantly impacted by tax considerations, but Fisher takes the contrarian 1970s view that the effects of taxes are "small or non-existent."

Although Fisher does not feel tax climates are important to states' economic growth, other authors contend the opposite. Bittlingmayer, Eathington, Hall and Orazem (2005) find in their analysis of several business climate studies that a state's tax climate does affect its economic growth rate, and that several indexes are able to predict growth. In fact, they found, "The State Business Tax Climate Index explains growth consistently." This finding was recently confirmed by Anderson (2006) in a study for the Michigan House of Representatives.

Bittlingmayer, et al, also found that relative tax competitiveness matters, especially at the borders, and therefore, indexes that place a high premium on tax policies better explain growth. Also, they observed that studies focused on a single topic do better at explaining economic growth at borders. Lastly, the article concludes that the most important elements of the business climate are tax and regulatory burdens on business (Bittlingmayer et al. 2005). These findings support the argument that taxes impact business decisions and economic growth, and they support the validity of the SBTICI.

Fisher and Bittlingmayer et al. hold opposing views about the impact of taxes on economic growth. Fisher finds support from Robert

7 Therese Poletti, "Incentive-Rich Arizona to House New Intel Plant," *San Jose Mercury News*, July 26, 2005.



Tannenwald of the Boston Federal Reserve, who argues that taxes are not as important to businesses as public expenditures. Tannenwald compares 22 states by measuring the after-tax rate of return to cash flow of a new facility built by a representative firm in each state. This very different approach attempts to compute the marginal effective tax rate (METR) of a hypothetical firm and yields results that make taxes appear trivial.

Tannenwald asserts, “While interjurisdictional rivalry is inducing states to cut taxes, demand is rising for state and local services such as education, health care, and law enforcement.” He concludes that business taxes exert only a small, highly uncertain effect on capital spending. States may be more likely to stimulate their economy by enhancing public services valued by business (Tannenwald 1996).

The taxes paid by businesses should be a concern to everyone because they are ultimately borne by individuals through lower wages, increased prices, and decreased shareholder value. States do not institute tax policy in a vacuum. Every change to a state’s tax system makes its business tax climate more or less competitive compared to other states, and makes the state more or less attractive to business. Ultimately, anecdotal and empirical evidence, along with the cohesion of recent literature around the conclusion that taxes matter a great deal to business, show that the SBTCI is an important and useful tool for policymakers who want to make their states’ tax systems welcoming to business.

## Methodology

The Tax Foundation’s 2009 State Business Tax Climate Index is a hierarchical structure built from five component indexes:

- The Corporate Tax Index
- The Individual Income Tax Index
- The Sales Tax Index
- The Unemployment Tax Index
- The Property Tax Index

Using the economic literature as our guide, we designed these five component indexes to score each state’s business tax climate on a scale of zero (worst) to 10 (best). Each component index is devoted to a major area of state taxation and each has two equally weighted sub-indexes, some of which include several categories and variables under them. Overall, there are 10 sub-indexes and 112 variables. The ranking of the states on each of

the five major component indexes is presented in Table 2.

The five component indexes are not weighted equally, as they are in many indexes. Rather, each component index is weighted based on the

**Table 2**

*Major Components of the State Business Tax Climate Index, FY 2009*

State	Overall Rank	Corporate Tax Index Rank	Individual Income Tax Index Rank	Sales Tax Index Rank	Unemployment	
					Insurance Tax Index Rank	Property Tax Index Rank
Alabama	21	21	17	33	14	13
Alaska	4	27	1	4	47	27
Arizona	22	24	23	45	2	4
Arkansas	35	34	31	35	23	18
California	48	45	49	43	16	15
Colorado	13	15	14	12	19	6
Connecticut	37	18	25	25	21	49
Delaware	10	49	28	2	7	8
Florida	5	13	1	21	3	19
Georgia	27	8	30	16	20	36
Hawaii	24	11	38	29	11	9
Idaho	29	17	32	32	45	3
Illinois	23	28	10	39	43	41
Indiana	14	23	11	19	13	7
Iowa	44	46	46	26	35	33
Kansas	31	37	21	17	8	32
Kentucky	34	38	36	7	48	20
Louisiana	33	19	24	46	10	22
Maine	40	43	40	8	40	40
Maryland	45	14	50	10	31	34
Massachusetts	32	47	16	9	49	44
Michigan	20	48	15	11	46	25
Minnesota	41	44	39	40	38	17
Mississippi	19	10	18	34	5	29
Missouri	16	5	27	22	4	11
Montana	6	16	22	3	18	10
Nebraska	42	32	33	42	12	48
Nevada	3	1	1	44	42	16
New Hampshire	8	50	9	1	39	39
New Jersey	50	39	48	41	24	50
New Mexico	26	35	19	47	17	1
New York	49	22	43	49	44	45
North Carolina	39	26	37	38	6	37
North Dakota	30	30	35	27	34	5
Ohio	47	33	47	36	15	46
Oklahoma	18	7	26	31	1	23
Oregon	9	20	34	5	30	14
Pennsylvania	28	41	12	24	26	47
Rhode Island	46	40	42	30	50	43
South Carolina	25	9	29	13	41	26
South Dakota	2	1	1	37	37	12
Tennessee	17	12	8	48	32	38
Texas	7	42	7	28	9	30
Utah	11	6	13	23	27	2
Vermont	43	31	45	15	22	42
Virginia	15	4	20	6	29	28
Washington	12	36	1	50	36	21
West Virginia	36	25	41	20	33	24
Wisconsin	38	29	44	18	25	31
Wyoming	1	1	1	14	28	35

**Note:** Rankings do not average across to total. States without a given tax rank equally as number 1.

**Source:** Tax Foundation

variability of the 50 states' scores from the mean. The standard deviation of each component index is calculated and a weight for each component index is created from that measure. The result is a heavier weighting of those component indexes with greater variability.

This improves the explanatory power of the SBTICI because component indexes with higher standard deviations are those areas of tax law where some states have significant competitive advantages. Businesses that are comparing states for new or expanded locations must give greater emphasis to tax climates when the differences are large. On the other hand, component indexes in which the 50 state scores are clustered together, closely distributed around the mean, are those areas of tax law where businesses are more likely to de-emphasize tax factors in their location decisions.

For example, Delaware is known to have a significant advantage in sales tax competition because its tax rate of zero attracts businesses and shoppers from all over the mid-Atlantic region. That advantage and its drawing power increase every time a state in the region raises its sales tax. In contrast with this sales tax variability, unemployment insurance taxes are similar around the nation.

Therefore, the 50 scores on this component index are centered tightly around the mean, offering less competitive advantage from state to state. A ranking of these taxes has less importance, then, because a small change in one state's law could change its component index ranking dramatically, but at the same time tell businesses very little about the overall differential between states. The weights are as follows:

1. 29.96% —Individual Income Tax Index
2. 22.21% —Sales Tax Index
3. 20.10% —Corporate Tax Index
4. 15.57% —Property Tax Index
5. 12.16% —Unemployment Insurance Tax Index

Within each component index are two sub-indexes devoted to measuring the impact of the tax rates and the tax base. These are weighted equally, 50 percent each.

Each sub-index is composed of one or more variables. There are two types of variables: scalar variables and dummy variables. A scalar variable is one that can have any value between 0 and 10. If a sub-index is composed only of scalar variables, then they are weighted equally.

A dummy variable is one that has only a value of 0 or 1. For example, a state either indexes its brackets for inflation or does not. Mixing scalar and dummy variables within a sub-index is problematic because the extreme valuation of a dummy can overly influence the results of the sub-index. To counter this effect, the Index weights scalar variables 80 percent and dummy variables 20 percent.

### Relative Versus Absolute Indexing

The 2009 State Business Tax Climate Index is designed as a *relative* index rather than an *absolute* or *ideal* index. In other words, each variable is ranked relative to the variable's range in other states. The relative scoring scale is from 0 to 10, with zero meaning not "worst possible" but rather worst among the 50 states.

For example the top rate for individual income taxation ranges from the lowest tax rate, 0.85 percent in New Hampshire<sup>8</sup> to the highest tax rate, 10.3 percent in California. New Hampshire therefore scores 10 in this sub-index, and California scores zero. All the other states that tax income range between these. Near to California is Iowa, with its top rate of 8.98 percent, yielding a low score of 1.08 in this sub-index. Near to New Hampshire is Illinois, with its flat tax rate of 3 percent scoring 7.73 in this sub-index. Oklahoma falls right in the middle with its 5.5 percent rate.

Many states' tax rates are so close to each other that an absolute index would not provide enough information about the differences between the states' tax systems, especially to pragmatic business owners who want to know what states have the best tax system in each region.

### Comparing States without a Tax

One problem associated with a relative scale, however, is that it is mathematically impossible to compare states with a given tax to states that do not have the tax. Clearly a zero rate is the lowest possible rate and the most neutral base, since it creates the most favorable tax climate for economic growth. The states that have a zero rate on individual income, corporate income or sales gain an immense competitive advantage. Therefore, states without a given tax receive a 10, and the Index measures all the other states against each other.

### Normalizing Final Scores

Another problem with using a relative scale within the component indexes is that the average scores across the five component indexes vary. This alters

8 Derived by combining its zero rate on wages with its 5% rate on interest and dividend income.

the value of not having a given tax across major indexes. For example, the unadjusted average score of the Corporate Tax Index is 7.20 while the average score of the Sales Tax Index is 6.04.

In order to solve this problem, scores on the five major component indexes are “normalized,” which brings the average score for all of them to 5.00—excluding states that do not have the given tax. This is accomplished by multiplying every state’s score by a constant value.

Once the scores are normalized it is possible to compare states across indexes. For example, because of normalization it is possible to say that Connecticut’s score of 5.26 on the Corporate Tax Index is better than its score of 3.06 on the Property Tax Index.

### Time Frame Measured by the SBTCI

Starting with the 2006 edition, the SBTCI has measured each state’s business tax climate as it stands at the beginning of the standard state fiscal year, July 1. Therefore, this edition is the 2009 SBTCI and represents the tax climate of each state as of July 1, 2008, the first day of fiscal year 2009 for most states.

### The District of Columbia

The District of Columbia (DC) is only included as an exhibit and does not affect the relative scores among states.

## Corporate Tax Index

The first of the five major component indexes that comprise the State Business Tax Climate Index measures the impact of each state’s principal tax on business activities. It is well established that the extent of business taxation can affect a business’s level of economic activity within a state. For example, Newman (1982) found that differentials in state corporate income taxes were a major factor influencing the movement of industry to southern states. Two decades later, with global investment greatly expanded, Agostini and Tulayasathien (2001) determined that a state’s corporate tax rate is the most relevant tax in the investment decisions of foreign investors.

The Corporate Tax Index consists of two distinct, equally weighted sub-indexes—one that measures the impact of the rate structure and one that measures the composition of the business tax base. These two sub-indexes are explained, with notes about which states scored particularly well

or poorly on each, and every variable included in the index is described in detail. The final score of the Corporate Tax Index is compiled from these variables and the entire Corporate Tax Index accounts for 20.10 percent of each state’s total score. See Tables 8, 9, 10 and 11 in Appendix 2 for details about how every state scores for each variable.

Most states levy standard corporate income taxes. Corporate income is generally defined as profit (gross receipts minus expenses). A growing number of states, however, impose taxes on the gross income of corporations with few or no deductions for expenses. In 2005, for example, Ohio enacted the Commercial Activities Tax (CAT) which taxes gross receipts in excess of \$1,000,000 at the rate of 0.26 percent (when fully phased in). Washington has the Business and Occupation Tax (B&O) which is a multi-rate tax (depending on industry) on the gross receipts of Washington businesses. Kentucky, New Jersey<sup>9</sup> and Texas have also recently enacted gross receipts taxes. In 2007, Michigan replaced its Single Business Tax (SBT) with a corporate income tax and a modified gross receipts tax called the Michigan Business Tax (MBT). The MBT taxes gross receipts less the purchases of goods from other firms. Illinois lawmakers also debated a proposal by Governor Blagojevich to swap the state’s corporate income tax for a tax on gross receipts, but it was ultimately defeated.

Since gross receipts taxes and corporate income taxes are levied on different bases, we separately compare gross receipts taxes to each other and corporate income taxes to each other.

For states with corporate income taxes, the state’s corporate tax rate sub-index is computed by assessing three key areas: the top tax rate, the level of taxable income at which the top rate kicks in, and the number of brackets. States that levy neither a corporate income tax nor a gross receipts tax clearly achieve a perfectly neutral system in regard to business income and so receive a perfect score.<sup>10</sup>

For states with gross receipts taxes—or their functional equivalent—the state’s corporate tax

### HAWAII

Hawaii significantly improved its unemployment insurance tax system for FY 2009, reducing the taxable wage base from \$35,300 to \$13,000. The taxable wage base represents the share of an employee’s wages on which an employer must pay UI tax; as such, a high taxable wage base is a disincentive to create jobs. Formerly, Hawaii had the highest taxable wage base in the country, while its new figure is close to the national average. Unfortunately, Hawaii’s property tax collections rose sharply, offsetting the UI improvement. Hawaii’s overall rank is 24th best in fiscal year 2009, down two spots from fiscal year 2008.

9 New Jersey’s gross receipts tax, called the Alternative Minimum Assessment (AMA), was phased out on July 1, 2007, for all companies except those companies who can claim protection under federal public law 86-272. Since these companies are mostly out of state, it is doubtful that New Jersey will be able to collect much revenue from them.

10 See Methodology for discussion of how the index scores states that have a given tax along with states that have not enacted one.

rate sub-index is computed by assessing two key areas: the gross receipts tax rate, and whether the gross receipts rate is an alternative assessment or a generally applicable tax. The latter variable was

included so that the states that levy a gross receipts tax as an alternative to the corporate income tax are not unduly penalized.

**Table 3**  
*Corporate Tax Index, 2006 – 2009*

State	FY 2009 State Business Tax Climate Index		FY 2008 State Business Tax Climate Index		Change from 2008 to 2009		FY 2007 State Business Tax Climate Index		FY 2006 State Business Tax Climate Index	
	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank
U.S.	5.00	–	5.00	–	5.00	–	5.00	–	5.00	–
Alabama	5.26	21	5.26	21	–0.01	0	5.21	21	5.22	22
Alaska	5.03	27	5.03	26	–0.01	–1	5.00	27	5.01	28
Arizona	5.12	24	5.13	24	–0.01	0	5.08	24	5.09	25
Arkansas	4.60	34	4.60	34	–0.01	0	4.56	36	4.57	37
California	4.28	45	4.29	45	–0.01	0	4.45	40	4.46	40
Colorado	5.59	15	5.59	16	–0.01	1	5.63	15	5.64	15
Connecticut	5.27	18	5.27	18	–0.01	0	4.99	28	5.34	18
Delaware	3.77	49	3.77	48	0.00	–1	4.04	48	4.05	47
Florida	5.75	13	5.76	14	–0.01	1	5.71	14	5.71	14
Georgia	5.93	8	5.94	9	–0.01	1	5.99	6	6.00	6
Hawaii	5.81	11	5.81	12	–0.01	1	5.86	9	5.87	9
Idaho	5.29	17	5.29	17	–0.01	0	5.26	19	5.27	20
Illinois	4.98	28	4.99	28	–0.01	0	4.95	30	4.96	30
Indiana	5.19	23	5.20	22	–0.01	–1	5.16	22	5.17	23
Iowa	4.28	46	4.28	46	–0.01	0	4.26	46	4.27	43
Kansas	4.56	37	4.57	38	–0.01	1	4.53	38	4.53	39
Kentucky	4.51	38	4.51	39	–0.01	1	4.39	43	4.89	33
Louisiana	5.26	19	5.27	19	–0.01	0	5.33	18	5.33	19
Maine	4.40	43	4.41	43	–0.01	0	4.37	44	4.38	42
Maryland	5.59	14	5.98	7	–0.39	–7	5.93	7	5.94	7
Massachusetts	4.17	47	4.18	47	–0.01	0	4.15	47	4.15	45
Michigan	4.06	48	3.29	49	0.78	1	3.47	49	3.47	49
Minnesota	4.33	44	4.34	44	–0.01	0	4.31	45	4.23	44
Mississippi	5.83	10	5.94	10	–0.11	0	5.88	8	5.89	8
Missouri	6.27	5	6.28	5	–0.01	0	5.83	10	5.84	10
Montana	5.44	16	5.64	15	–0.20	–1	5.59	16	5.60	16
Nebraska	4.68	32	4.70	31	–0.03	–1	4.66	34	4.67	35
Nevada	10.00	1	10.00	1	0.00	0	10.00	1	10.00	1
New Hampshire	2.95	50	2.99	50	–0.04	0	2.88	50	3.56	48
New Jersey	4.48	39	4.48	40	–0.01	1	4.45	41	3.01	50
New Mexico	4.59	35	4.60	35	–0.01	0	4.55	37	4.56	38
New York	5.22	22	5.13	23	0.08	1	5.09	23	5.10	24
North Carolina	5.05	26	5.06	25	–0.01	–1	5.01	25	5.02	26
North Dakota	4.93	30	4.83	30	0.11	0	4.98	29	4.99	29
Ohio	4.64	33	4.58	36	0.06	3	4.48	39	4.14	46
Oklahoma	5.96	7	5.97	8	–0.01	1	5.72	13	5.73	13
Oregon	5.26	20	5.27	20	–0.01	0	5.22	20	5.23	21
Pennsylvania	4.43	41	4.43	41	–0.01	0	4.40	42	4.41	41
Rhode Island	4.46	40	4.63	33	–0.18	–7	4.60	35	4.60	36
South Carolina	5.87	9	5.88	11	–0.01	2	5.82	11	5.83	11
South Dakota	10.00	1	10.00	1	0.00	0	10.00	1	10.00	1
Tennessee	5.79	12	5.80	13	–0.01	1	5.75	12	5.76	12
Texas	4.42	42	4.43	42	–0.01	0	5.35	17	5.36	17
Utah	6.04	6	6.05	6	–0.01	0	6.24	4	6.25	4
Vermont	4.78	31	4.68	32	0.10	1	4.95	31	4.96	31
Virginia	6.33	4	6.34	4	–0.01	0	6.18	5	6.19	5
Washington	4.57	36	4.57	37	–0.01	1	4.84	33	4.85	34
West Virginia	5.05	25	5.00	27	0.05	2	5.01	26	5.02	27
Wisconsin	4.93	29	4.94	29	–0.01	0	4.90	32	4.91	32
Wyoming	10.00	1	10.00	1	0.00	0	10.00	1	10.00	1
D.C.	4.59	–	4.59	–	–0.01	–	3.97	–	3.98	–

**Note:** The higher the score, the more favorable a state's tax system is for business. All scores are for fiscal years.

**Source:** Tax Foundation



States that do impose a corporate tax generally will score well if they have a low rate. States with a high rate or a complex, multiple-rate system score poorly.

To compute the parallel sub-index for the corporate tax base, three broad areas are assessed: tax credits, treatment of net operating losses, and an “other” category that includes variables such as conformity to the Internal Revenue Code, protections against double taxation, and the taxation of “throwback” income provisions, among others. States that score well on the corporate tax base sub-index generally will have few business tax credits, generous carry-back and carry-forward provisions, deductions for net operating losses, conformity to the Internal Revenue Code, and provisions for alleviating double taxation.

The three states with no general corporate tax are Nevada, South Dakota and Wyoming, and they receive the highest scores on the Corporate Tax Index.

Among those states that do levy general corporate taxes, the five states with the best systems are Virginia, Missouri, Utah, Oklahoma and Georgia. Each has a relatively low, single-rate system that applies to a broad base of business activity. South Carolina, Mississippi, Hawaii and Tennessee also score well.

By contrast, New Hampshire has the lowest score because it has a high income tax rate, 8.5 percent on income over \$50,000, and a value added style tax called the Business Enterprise Tax. The other states rounding out the bottom ten are Delaware, Michigan, Massachusetts, Iowa, California, Minnesota, Maine, Texas and Pennsylvania. In general, these states have complex, multi-rate systems with high top marginal tax rates. Other factors that contribute to poor rankings are numerous tax credits, restrictive treatment of net operating loss and the double taxation of income. In addition to New Hampshire, only Delaware, Michigan and Ohio (ranked 49<sup>th</sup>, 48<sup>th</sup> and 33<sup>rd</sup> respectively) levy both corporate income and gross receipts-style taxes simultaneously. Although Ohio is currently phasing out its franchise tax (essentially equivalent to a corporate income tax) through 2010, until then it will have two corporate tax structures: the franchise tax and the new gross receipts tax, called

the Corporate Activities Tax (CAT). If Ohio maintains the low 0.26 percent CAT rate, the full phase-out of the franchise tax will improve its score on the corporate component index.

Kentucky's gross receipts tax is an alternative tax, explained below. See Table 3 for a ranking of all the states.

## Sub-Index #1: The Corporate Tax Rate

The corporate tax rate sub-index is designed to gauge how a state's corporate income tax top rate, bracket structure, and gross receipts rate affect its competitiveness compared to other states, as the extent of taxation can affect a business's level of economic activity within a state (Newman 1982).

A state's corporate tax is levied in addition to the federal corporate income tax rate, which varies from 15 percent on the first dollar of income to a top rate of 35 percent.<sup>11</sup> This top rate is higher than the corporate income tax rate in all but a few industrial nations. In many states, federal and state corporate tax rates combine to levy the highest corporate tax rates in the world.<sup>12</sup>

On the other hand, there are three states that levy neither a corporate income tax nor a gross receipts tax: Nevada, South Dakota and Wyoming. These states automatically score a perfect 10 for this sub-index. Therefore, this section ranks the remaining 47 states relative to each other. A discussion of each variable follows.

### The Top Rate

Iowa's 12 percent corporate income tax rate qualifies for the worst ranking among states that levy one, followed by Pennsylvania's 9.99 percent rate. Other states with comparatively high corporate income tax rates are the District of Columbia (9.975 percent), Minnesota (9.8 percent), Massachusetts (9.5 percent), Alaska (9.4 percent), New Jersey (9.36 percent including a 4 percent surcharge) and Rhode Island (9 percent). States that levy just a gross receipts tax are counted as having a top corporate income tax rate of zero percent.

By contrast, Colorado's 4.63 percent is the lowest nationally. Other states with comparatively low top corporate tax rates are Mississippi (5 percent), South Carolina (5 percent), and Utah (5 percent).

11 For firms with less than \$50,000 in taxable income, the rate is 15 percent. The rate is 25 percent on the next \$25,000 in income; and for firms with taxable income between \$75,000 and \$10,000,000, the rate is 34 percent. Above that, the marginal rate is 35 percent, although “manufacturing” firms benefited from a preference equal to one percentage point in 2005. State taxes are deductible on the federal return so the statutory rates at the federal and state levels cannot be simply added.

12 See Chris Atkins and Scott Hodge, “U.S. Lagging Behind OECD Corporate Tax Trends,” *Tax Foundation Fiscal Fact*, No. 96 (July 24, 2007), located at <http://www.taxfoundation.org/publications/show/72501.html>.

Among states that levy gross receipts taxes, Texas's is the highest (1.0 percent), followed by Michigan (0.98 percent) New Hampshire (0.75 percent), Delaware (0.576 percent), Washington (0.484 percent), Ohio (0.208 percent), and Kentucky (0.095 percent).<sup>13</sup> Ohio's rate is phasing

## UTAH

Utah saw its overall rank rise five spots to 11<sup>th</sup> this year, primarily driven by a major overhaul of its income tax. The state replaced its graduated income tax with a 5% flat rate tax. This favorable change improved its income tax from the middle of the pack to 13<sup>th</sup> best—or 4<sup>th</sup> best among the 41 states that apply a general tax to personal income.

in and will reach 0.26 percent in 2009. Because gross receipts taxes vary widely in deductions available, comparing their rates directly is a crude metric; we compensate for this in the corporate income tax base sub-index, where we give states like Texas credit for allowing certain deductions for cost of goods sold and employee compensation, which partly offset the high rate.

### The Graduated Rate Structure

Two variables are used to measure the economic drag created by multiple-rate corporate income tax systems: the income level at which the highest tax rate starts to apply and the number of tax brackets. Thirty-two states and the District of Columbia have flat, single-rate systems, and they score best. Flat-rate systems are consistent with the sound tax principles of simplicity and neutrality. A flat system does not impact the economic decisions of businesses as they become more successful and earn additional income.

#### The Top Bracket

This variable measures how soon a state's tax system applies its highest corporate income tax rate. States score best if their top rate kicks in at a low level of income, since the lower the top rate kicks in, the more the system is like a flat tax. However, states also score well if their top rate kicks in at a very high level of income since fewer companies pay tax at that rate. New Mexico (\$1,000,000), Iowa (\$250,000), Vermont (\$250,000) and Maine (\$250,000) score the best since their top rates kick in at high levels of income.<sup>14</sup> States with flat systems also score best since their top rate kicks in at zero. States where the top rate kicks in at medium levels of income score the worst. Arkansas, Kentucky, Hawaii and New Jersey all score poorly because their top rates kick in at \$100,000.

#### The Number of Brackets

An income tax system creates changes in behavior when the taxpayer's income reaches the end of one

tax rate bracket and moves into a higher bracket. At such a break point, incentives change, and as a result, numerous rate changes are more economically harmful than a single-rate structure. This variable is intended to measure the disincentive effect the corporate income tax has on rising incomes. States that score the best on this variable are the 32 states and the District of Columbia that have a single-rate system. Alaska's 10-bracket system earns the worst score in this category. Other states with multi-bracket systems include Arkansas (6 brackets), North Dakota (5 brackets) and Louisiana (5 brackets).

## Sub-Index #2: The Corporate Tax Base

This sub-index measures the economic impact of each state's definition of what should be subject to corporate taxation.

Under a corporate income tax, three criteria used to measure the competitiveness of each state's tax base are given equal weight: the availability of certain credits, deductions and exemptions; the ability of taxpayers to deduct net operating losses; and a host of smaller tax base issues that combine to make up the other third of the corporate tax base.

Under a gross receipts tax, these tax base criteria are replaced by the availability of deductions from gross receipts for employee compensation costs and cost of goods sold. States are rewarded for granting these deductions because they diminish the greatest disadvantage of using gross receipts as the base for corporate taxation: the uneven effective tax rates that various industries pay, depending on how many levels of production are hit by the tax.

The three states that levy neither a corporate income tax nor a gross receipts tax—Nevada, South Dakota and Wyoming—receive a perfect score for this sub-index. Of the 47 states with one or both taxes, Missouri, Virginia, Maryland, Hawaii and Oklahoma receive the best scores. By contrast, New Hampshire has the worst score, followed by Arkansas, Ohio, Kansas, California and Washington.

### Net Operating Losses

The corporate income tax is designed to tax only the profits of a corporation. However, a yearly profit snapshot may not fully capture a corporation's true profitability. For example, a

13 Kentucky's gross receipts tax is an alternative assessment. Companies doing business in Kentucky compute liability under the corporate income tax and the gross receipts tax, and pay whichever tax is higher.

14 States whose tax brackets begin at an income threshold that is more than one standard deviation higher than the average threshold receive a perfect score.

corporation in a highly cyclical industry may look very profitable during boom years but lose substantial amounts during bust years. When examined over the entire business cycle, the corporation may actually have an average profit margin.

The deduction for net operating losses (NOL) helps ensure that, over time, the corporate income tax is a tax on average profitability. Without the NOL deduction, corporations in cyclical industries pay much higher taxes than those in stable industries, even assuming identical average profits over time. Put simply, the NOL deduction helps level the playing field among cyclical and non-cyclical industries. The federal government currently allows a two-year carry-back cap and a 20-year carry-forward cap, and these two variables are taken into account as the index assesses state tax systems.

#### *Number of Years Allowed for Carry-Back and Carry-Forward*

This variable measures the number of years allowed on a carry-back or carry-forward of an NOL deduction. The longer the overall time span, the higher the probability that the corporate income tax is being levied on the corporation's average profitability. Generally, states entered 2009 with better treatment of the carry-forward (up to a maximum of 20 years) than the carry-back (up to a maximum of three years).

#### *Caps on the Amount of Carry-Back and Carry-Forward*

When companies have a bigger NOL than they can deduct in one year, most states permit them to carry deductions of any amount back to previous years' returns or forward to future returns. States that limit those amounts are downgraded in the Index. Five states limit the amount of carry-backs: Delaware, Idaho, New York, Utah and West Virginia. Only Pennsylvania and New Hampshire limit carry-forwards. As a result, these states score poorly in this variable.

#### **Tax Credits**

Many states provide tax credits to lower the effective tax rates for certain industries and/or investments, often for large firms from out of state who are considering a move. Lawmakers create these deals under the banner of job creation and economic development, but the truth is that if a state needs to offer such packages, it is most likely covering for a bad business tax climate. Tax credits complicate the tax system, narrow the tax base, drive up tax rates for companies that do not qualify and distort the free market.

A far more effective approach is to systematically improve the business tax climate for the long term so as to improve the state's competitiveness as compared to other states. Thus, this component index rewards those states that do not offer the following tax credits, and states that offer them score poorly.

#### *Investment Tax Credits*

Investment tax credits typically offer an offset against tax liability if the company invests in new property, plants, equipment, or machinery in the state offering the credit. Sometimes, the new investment will have to be "qualified" and approved by the state's economic development office. Investment tax credits distort the free market by encouraging investment in new property as opposed to the renovation of old property.

#### *Job Tax Credits*

Job tax credits typically offer an offset against tax liability if the company creates a specified number of jobs over a specified period of time. Sometimes, the new jobs will have to be "qualified" and approved by the state's economic development office, allegedly to prevent firms from claiming that jobs shifted were jobs added. Even if administered efficiently, which is uncommon, job tax credits can misfire in a number of ways. They push businesses whose economic position would be best served by spending more on new equipment or marketing to hire new employees instead. They reward businesses who are expanding anyway, punishing firms that are already struggling. Thus, states that offer such credits score poorly on the Index.

#### *Research and Development (R&D) Tax Credits*

R&D tax credits reduce the amount of tax due by a company that invests in "qualified" research and development activities. The theoretical argument for R&D tax credits is that they encourage the kind of basic research that is not economically justifiable in the short run but that is better for society in the long run. In practice, we find that its negative side effects—greatly complicating the tax system and establishing a government agency as the arbiter of what types of research meet a criterion so difficult to assess—far outweigh the potential benefits. Thus, states that offer such credits score poorly on the Index.

#### **Gross Receipts Tax Deductions**

Proponents of gross receipts taxation invariably praise the steadier flow of tax receipts into government coffers, in comparison with the

fluctuating revenue generated by corporate income taxes, but this stability comes at a great cost. Firms with few steps in production are relatively lightly taxed under a gross receipts tax, and vertically-integrated, high-margin firms prosper. The pressure of this economic imbalance often leads lawmakers to enact separate rates for each industry, an inevitably unfair and inefficient process.

Two reforms that states can make to mitigate this damage are to permit deductions from gross receipts for employee compensation costs and cost of goods sold, effectively moving toward a regular corporate income tax.

Delaware, Ohio and Washington score the worst because they do not offer full deductions for either cost of goods sold or employee compensation. However, Kentucky and New Hampshire offer a deduction for cost of goods sold, Michigan a deduction for cost of goods sold and a limited deduction for employee compensation, and Texas a deduction for either the cost of goods sold or compensation.

## Other Significant Features

### *Federal Income Used as State Tax Base*

States that use federal definitions of income help reduce the tax compliance burden on their taxpayers.<sup>15</sup> Two states do not conform to federal definitions of corporate income—Arkansas and Mississippi—and they score poorly.

### *Allowance of Federal ACRS and MACRS Depreciation*

The vast array of federal depreciation schedules is, by itself, a tax complexity nightmare for businesses. The specter of having 50 different schedules would be a disaster from a tax complexity standpoint. This variable measures the degree to which states have adopted the federal ACRS and MACRS depreciation schedules.<sup>16</sup> Two states that add complexity by failing to fully conform to the federal system are California and Michigan.

### *Deductibility of Depletion*

The deduction for depletion works similarly to depreciation, but it applies to natural resources. As with depreciation, tax complexity would be staggering if all 50 states imposed their own

depletion schedules. This variable measures the degree to which states have adopted the federal depletion schedules.<sup>17</sup> Eleven states are penalized because they do not fully conform to the federal system: Alabama, Minnesota, Oregon and Wisconsin do not comply while Alaska, Delaware, Iowa, Louisiana, New Hampshire, North Carolina and Texas only partially comply.

### *The Alternative Minimum Tax*

The federal Alternative Minimum Tax (AMT) was created to ensure that all taxpayers paid some minimum level of taxes every year. Unfortunately, it creates a parallel tax system to the standard corporate income tax code. Evidence shows that the AMT does not increase efficiency or improve fairness in any meaningful way. It nets little money for the government, imposes compliance costs that in some years are actually larger than collections, and encourages firms to cut back or shift their investments (Chorvat and Knoll 2002). As such, states that have mimicked the federal AMT put themselves at a competitive disadvantage through needless tax complexity.

Seven states have an AMT on corporations—Alaska, California, Florida, Iowa, Maine, Minnesota and New York—and score poorly.<sup>18</sup>

### *Deductibility of Taxes Paid*

This variable measures the extent of double taxation on income used to pay foreign taxes, i.e., paying a tax on money the taxpayer has already mailed to foreign taxing authorities. States can avoid this double taxation by allowing the deduction of taxes paid to foreign jurisdictions. Twenty-one states allow deductions for foreign taxes paid and score well. The remaining 26 states with corporate income taxation do not allow deductions for foreign taxes paid and thus score poorly.

### *Indexation of the Tax Code*

For states that have multiple-bracket income tax codes, it is important to index the brackets for inflation. That prevents de facto tax increases on the nominal increase in income due to inflation. Put simply, this “inflation tax” results in higher tax burdens on taxpayers, usually without their knowledge or consent. Fifteen states do not index their corporate income tax brackets<sup>19</sup>: Alaska,

15 This is not an endorsement of the economic efficiency of the federal definition of corporate income.

16 This is not an endorsement of the federal ACRS/MACRS depreciation system. It is well known that federal tax depreciation schedules often bear little resemblance to actual economic depreciation rates.

17 This is not an endorsement of the economic efficiency of the federal depletion system.

18 Five of these states impose both corporate and individual AMTs: California, Iowa, Maine, Minnesota and New York. An individual AMT sub-index is contained within the Individual Income Tax Index.

19 This variable only looks at states that have statutory automatic provisions to index for inflation. This does not reflect recent or ongoing legislative activity.



Arkansas, Hawaii, Iowa, Kansas, Kentucky, Louisiana, Maine, Mississippi, Nebraska, New Jersey, New Mexico, North Dakota, Ohio and Vermont.<sup>20</sup>

### Throwback

To reduce the double taxation of corporate income, states use an apportionment system that seeks to determine how much of a company's income a state has the right to tax. Generally, states require a company with nexus (that is, sufficient connection to the state to justify the state's right to tax its income) to apportion its income to the state based on in-state property, payroll and sales compared to total property, payroll and sales.

Among the 50 states, there is little harmony in apportionment formulas. Many states weight the three factors equally while others weight the sales factor more heavily (a recent trend in state tax policy). Since many businesses make sales into states where they do not have nexus, businesses can end up with "nowhere income," income that is not taxed by any state. To counter this phenomenon, many states have adopted what are called throwback rules because they identify nowhere income and throw it back into a state where it will be taxed.

Throwback rules add yet another layer of tax complexity. Since two or more states can theoretically lay claim to "nowhere" income, rules have to be created and enforced to decide who gets to tax it. States with corporate income taxation are almost evenly divided between those with and without throwback rules. Twenty-three states do not have them, and 24 states and the District of Columbia do.

## Individual Income Tax Index

The individual income tax code in each state is also a consideration for business. One important reason is that a significant number of businesses, including sole proprietorships, partnerships and S-corporations, report their income through the individual income tax code. Indeed, the number of individuals filing federal tax returns with business income has nearly doubled over the past 20 years, from 13.3 million in 1980 to 25.5 million in 2002.<sup>21</sup>

Taxes can have a significant impact on an individual's decision to become a self-employed

entrepreneur. Gentry and Hubbard (2004) found, "While the level of the marginal tax rate has a negative effect on entrepreneurial entry, the progressivity of the tax also discourages entrepreneurship, and significantly so for some groups of households." (p. 21) Using education as a measure of potential for innovation, Gentry and Hubbard found that a progressive tax system "discourages entry into self-employment for people of all educational backgrounds." Moreover, citing Carroll, Holtz-Eakin, Rider and Rosen (2000), Gentry and Hubbard contend, "Higher tax rates reduce investment, hiring, and small business income growth." (p. 7) Less neutral individual income tax systems, therefore, hurt entrepreneurship and a state's business tax climate.

Another important reason individual income tax rates are critical for business is the cost of labor. Labor typically constitutes a major business expense, so anything that hurts the labor pool will also affect business decisions and the economy. Complex, poorly designed tax systems that extract an inordinate amount of tax revenue are known to reduce both the quantity and quality of the labor pool. This finding was supported by Wasylenko and McGuire (1985), who found that individual income taxes affect businesses indirectly by influencing the location decisions of individuals. A progressive, multi-rate income tax exacerbates this problem by systematically ratcheting up the marginal tax rate at higher levels of income. Thus the tax system continually reduces the value of work vis-à-vis the value of leisure.

For example, suppose a worker has to choose between one hour of additional work worth \$10 and one hour of leisure which to him is worth \$9.50. A rational person would choose to work for another hour. But if a 10-percent income tax rate reduces the after-tax value of labor to \$9.00, then a rational person would stop working and take the hour to pursue leisure. Workers earning higher wages, \$30 an hour for example, that face progressively higher marginal tax rates, 20 percent for instance, are more likely to be discouraged from working additional hours. In this scenario, the worker's after-tax wage is \$24 an hour; therefore those workers that value leisure more than \$24 an

### NORTH CAROLINA

With Maryland's dramatic fall into the bottom ten tax climates (see above), one of last year's ten worst had to rise out. That state was North Carolina, rising from 42<sup>nd</sup> in last year's index to 39<sup>th</sup> this year. In addition to benefiting from Maryland's fall, North Carolina completed a phase-down of its top income tax rate to 7.75%, from 8.0% last year and 8.25% previously. Despite improvement on its income tax, North Carolina still compares unfavorably to its neighbors, featuring the worst business tax climate in the South.

20 States with a single-rate system do not have any brackets to adjust for inflation and are therefore treated as if they were indexation states.

21 Scott A. Hodge and J. Scott Moody, "Wealthy American and Business Activity," *Tax Foundation Special Report*, No. 131, August 1, 2004.

hour will choose not to work. Since the after-tax wage is \$6 lower than the pre-tax wage in this example, compared to only \$1 lower in the previous example, more workers will choose leisure. In the aggregate, the income tax reduces the available labor supply.<sup>22</sup>

Aside from measuring the economic impact of each state's individual income tax on wage earners, the Individual Income Tax Index measures the impact on non-corporate businesses. Because sole proprietorships, partnerships and S-corporations report business income not on corporate tax returns but on individual tax returns, the structure of the individual income tax code is critical to the business tax climate for these firms.

The individual rate sub-index measures the impact of tax rates on the marginal dollar of individual income using three criteria: the top tax rate, the graduated rate structure, and standard deductions and exemptions which are treated as a zero percent tax rate. The rates and brackets used are for a single taxpayer, not a couple filing a joint return.<sup>23</sup>

Like the Corporate Tax Index, the Individual Income Tax Index is comprised of two complex sub-indexes measuring the states' tax rate structures and tax bases. Tax rate structure is assessed in four key areas: the states' top marginal tax rates (including local option income rates if a state allows them), the starting points of their top brackets, the number of brackets and the average width of brackets. States that do not impose an individual income tax receive a perfect score, and states that do will generally score well if they have a flat, low tax rate with few deductions and exemptions. States that score poorly have complex, multiple-rate systems.

States' tax bases are assessed on a variety of factors, including how the tax code treats married couples, the lengths to which a tax code goes to prevent double taxation, and whether the code is indexed for inflation. States that score well protect married couples from being taxed more severely than if they had filed as two single people. They also protect taxpayers from double taxation by recognizing LLCs and S-corps under the individual tax code and indexing their brackets, exemptions and deductions for inflation.

The seven states without an individual income tax are, naturally, the highest-scoring

states on this component index: Alaska, Florida, Nevada, South Dakota, Texas, Washington and Wyoming. New Hampshire and Tennessee also score well because, while they levy a significant tax on individual income in the form of interest and dividends, they do not tax wages and salaries. Of the 41 states that do have a broad-based individual income tax, Illinois, Indiana, Pennsylvania, Utah and Colorado score highly because they have a single, low tax rate. Utah phased out its graduated income tax over the last several years, with the flat tax fully phasing in on January 1, 2008. This improved Utah's income tax rank from 25<sup>th</sup> on last year's index to 13<sup>th</sup> this year.

On the other hand, Maryland has the worst score because of a large income tax increase enacted for 2008. The state added four new income tax brackets, taking the top tax rate to 9.23%, including local option taxes. The income tax now has nine brackets (including the standard deduction as a zero bracket). The brackets are not indexed to inflation, and are not doubled for married couples, imposing a large marriage penalty.

California scores second worst because of its highest-in-the-nation top rate of 10.3 percent that kicks in at incomes over \$1 million. The so-called "millionaires tax" bracket is not doubled for married couples and therefore imposes a large marriage penalty. California has seven separate brackets, and its system is one of the most progressive in the country. However, California's brackets are mostly indexed for inflation and its marriage penalty is smaller than Maryland's, and as a result it does not score dead last.

The other states rounding out the bottom ten are New Jersey, Ohio, Iowa, Vermont, Wisconsin, New York, Rhode Island and West Virginia. The individual income tax systems in these states are plagued by high tax rates and progressive bracket structures. They generally fail to index their brackets, exemptions and deductions for inflation, do not allow for deductions of foreign or other state taxes, penalize married couples filing jointly, and do not recognize LLCs and S-Corps. See Table 4 for a 50-state ranking.

Similar to the Corporate Tax Index, the Individual Income Tax Index consists of two equally weighted sub-indexes—one to measure the impact of the rate structure and one to measure the competitiveness of each state's tax base. These two sub-indexes are defined below, with every

22 For a more detailed explanation, see Fleenor and Moody (1999).

23 In many states, tax brackets, deductions and exemptions for joint filers are simply twice that of a single filer. Therefore, the relative economic impacts are similar. For states where they are not doubled, there exists a "marriage penalty" which is measured in the marriage penalty category of the tax base sub-index.

variable discussed, and states that score especially well or poorly are noted. The final score of the Individual Income Tax Index accounts for 29.96

percent of each state's total score on the State Business Tax Climate Index. See Tables 12, 13 and 14 in the appendix.

**Table 4**  
*Individual Income Tax Index, 2006 – 2009*

State	FY 2009 State Business Tax Climate Index		FY 2008 State Business Tax Climate Index		Change from 2008 to 2009		FY 2007 State Business Tax Climate Index		FY 2006 State Business Tax Climate Index	
	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank
U.S.	5.00	–	5.00	–	5.00	–	5.00	–	5.00	–
Alabama	5.36	17	5.43	17	–0.07	0	5.47	17	5.48	17
Alaska	10.00	1	10.00	1	0.00	0	10.00	1	10.00	1
Arizona	5.14	23	5.21	22	–0.07	–1	5.14	25	5.11	25
Arkansas	4.87	31	4.83	34	0.05	3	4.76	33	4.78	32
California	2.51	49	1.93	50	0.58	1	1.99	50	1.99	50
Colorado	6.41	14	6.50	14	–0.09	0	6.56	14	6.58	14
Connecticut	5.07	25	5.45	16	–0.38	–9	5.49	16	5.50	16
Delaware	4.95	28	4.94	29	0.01	1	4.92	31	4.94	31
Florida	10.00	1	10.00	1	0.00	0	10.00	1	10.00	1
Georgia	4.91	30	4.97	28	–0.06	–2	5.01	26	5.03	27
Hawaii	4.38	38	4.46	37	–0.08	–1	4.22	42	4.23	42
Idaho	4.86	32	4.93	30	–0.07	–2	5.01	27	5.03	26
Illinois	6.97	10	6.82	11	0.14	1	6.85	12	6.87	12
Indiana	6.72	11	6.88	10	–0.16	–1	6.94	10	6.97	10
Iowa	3.70	46	3.70	45	0.00	–1	3.84	45	4.12	43
Kansas	5.20	21	5.26	20	–0.05	–1	5.31	20	5.34	20
Kentucky	4.78	36	4.75	35	0.03	–1	4.26	41	4.35	41
Louisiana	5.09	24	5.13	24	–0.04	0	5.18	23	5.20	22
Maine	4.33	40	4.40	39	–0.06	–1	4.48	37	4.50	38
Maryland	2.06	50	4.42	38	–2.36	–12	4.54	36	4.55	36
Massachusetts	6.41	16	6.35	15	0.07	–1	6.45	15	6.47	15
Michigan	6.41	15	6.61	13	–0.20	–2	6.74	13	6.77	13
Minnesota	4.34	39	4.39	40	–0.06	1	4.47	38	4.50	37
Mississippi	5.35	18	5.41	18	–0.06	0	5.44	18	5.46	18
Missouri	4.96	27	4.99	27	–0.04	0	4.98	29	4.99	29
Montana	5.15	22	5.19	23	–0.04	1	5.26	22	5.28	21
Nebraska	4.85	33	4.91	32	–0.07	–1	4.61	35	4.63	35
Nevada	10.00	1	10.00	1	0.00	0	10.00	1	10.00	1
New Hampshire	7.55	9	7.65	9	–0.10	0	7.20	9	7.86	8
New Jersey	3.18	48	2.86	49	0.31	1	2.94	49	3.00	47
New Mexico	5.29	19	5.26	21	0.04	2	5.29	21	5.12	24
New York	4.22	43	4.28	42	–0.06	–1	4.03	44	2.86	49
North Carolina	4.46	37	4.08	44	0.38	7	4.08	43	4.11	44
North Dakota	4.78	35	4.56	36	0.21	1	4.61	34	4.68	34
Ohio	3.22	47	2.98	48	0.24	1	2.94	48	2.96	48
Oklahoma	5.01	26	5.01	26	0.00	0	4.91	32	4.76	33
Oregon	4.84	34	4.90	33	–0.07	–1	4.95	30	4.96	30
Pennsylvania	6.61	12	6.69	12	–0.08	0	6.91	11	6.93	11
Rhode Island	4.32	42	3.69	46	0.64	4	3.63	47	3.24	46
South Carolina	4.93	29	4.92	31	0.01	2	4.98	28	5.00	28
South Dakota	10.00	1	10.00	1	0.00	0	10.00	1	10.00	1
Tennessee	7.64	8	7.74	8	–0.10	0	7.80	8	7.82	9
Texas	9.44	7	9.44	7	0.00	0	9.44	7	9.44	7
Utah	6.59	13	5.11	25	1.48	12	5.17	24	5.19	23
Vermont	3.81	45	3.58	47	0.23	2	3.69	46	3.77	45
Virginia	5.24	20	5.31	19	–0.07	–1	5.32	19	5.34	19
Washington	10.00	1	10.00	1	0.00	0	10.00	1	10.00	1
West Virginia	4.33	41	4.31	41	0.03	0	4.34	39	4.36	40
Wisconsin	4.21	44	4.22	43	–0.01	–1	4.31	40	4.36	39
Wyoming	10.00	1	10.00	1	0.00	0	10.00	1	10.00	1
D.C.	4.40	–	4.34	–	0.07	–	4.41	–	4.35	–

**Note:** The higher the score, the more favorable a state's tax system is for business. All scores are for fiscal years.

**Source:** Tax Foundation

## Sub-Index #1: The Individual Income Tax Rate

The sub-index compares the 43 states that tax individual income after setting aside the seven states that levy no individual income tax and therefore receive perfect scores: Alaska, Florida, Nevada, South Dakota, Texas, Washington and Wyoming. Among the other 43, two equally weighted variables are considered to calculate the rate sub-index score: the top tax rate and the graduated rate structure. New Hampshire,

Tennessee, Illinois, Pennsylvania, Indiana and Colorado scored the best. California, Maryland, Ohio, Iowa and Vermont had the five worst scores. A discussion of each variable follows.

### The Top Marginal Tax Rate

California imposes the highest top statutory rate of 10.3 percent, which it imposes on incomes over \$1 million. Other states with high top tax rates include Vermont (9.5 percent), Oregon (9.36 percent), Iowa (9.28 percent) and Maryland (9.23 percent).

Among those states with the lowest rates, New Hampshire (0.85 percent) and Tennessee (1.02 percent) score the best.<sup>24</sup> Other states with relatively low top rates include: Illinois (3.0 percent of federal AGI); Pennsylvania (4.32 percent); Arizona (4.54 percent); Indiana (4.56 percent of federal AGI); Colorado

(4.63 percent of federal taxable income); Connecticut and Mississippi (5 percent).

If only state-level tax rates were considered, Maryland would not be in the group of states with the highest top rates. However, municipal and county-level income taxes are also counted and as a result, Maryland's average local rate of 2.98

percent is added to its 6.25 percent top state-level rate—for a combined rate of 9.23 percent.<sup>25</sup>

Other states with local option income taxes added to the top state rate include: Alabama (0.19 percent added to for a total of 5.19 percent), Arkansas (0.06 percent added for a total of 7.06 percent), Delaware (0.16 percent added for a total of 6.11 percent), Indiana (1.16 percent added for a total of 4.56 percent), Iowa (0.30 percent added for a total of 9.28 percent), Kentucky (0.76 percent added for a total of 6.76 percent), Michigan (0.44 percent added for a total of 4.79 percent), Missouri (0.12 added for a total of 6.12 percent), New Jersey (0.09 percent added for a total of 9.06 percent), New York (1.70 percent added for a total of 8.55 percent), Ohio<sup>26</sup> (1.82 percent added for a total of 8.06 percent), Oregon (0.36 added for a total of 9.36 percent) and Pennsylvania (1.25 percent added for a total of 4.32 percent). Even though Alabama, Indiana, Michigan and Pennsylvania allow for local income add-ons, they are still among the states with the lowest overall rates.

### Graduated Rate Structure

This sub-index measures the impact of a graduated individual income tax structure via three variables: the level of taxable income at which the top rate takes effect, the number of tax brackets and the average width of those brackets.

#### Top Tax Bracket Threshold

The income level at which a state's top rate kicks in determines what amount of income is subject to the top rate. States are rewarded for either taxing most income at the top rate (having a low income threshold for the top rate) or taxing very little income at the top rate (having a very high income threshold for the top rate). States whose top rate kicks in at low levels of income effectively have flat rate systems, and states where the kick-in is high have top rates that apply to few taxpayers.<sup>27</sup>

States with flat-rate systems score the best on this variable because their top rate kicks in at the

### RHODE ISLAND

Rhode Island is phasing in an optional flat-rate income tax. Filers may pay either under a traditional graduated-rate structure based on the federal income tax, or may pay a flat rate on all income with no deductions. This year's flat rate is 7.0%, falling by 0.5% per year until it reaches 5.5% in 2011. Because of this unusual structure, we score Rhode Island mostly based on the graduated system, but we substitute the optional flat rate in our variable for Rhode Island's "top rate." This is because a great many taxpayers in the top income bracket (which starts at \$349,700 of income) will chose to file under the optional flat system, instead of paying at the top marginal rate of 9.9%. Rhode Island should see its score improve each year as the flat rate falls; this year, Rhode Island rated 46<sup>th</sup> out of 50 states overall, improved from 49<sup>th</sup> last year. Without the optional flat tax, the state would score dead last overall.

24 New Hampshire and Tennessee both tax only interest and dividends. To make their top tax rates comparable to other states, the Index calculates the rate needed to collect the same revenue as a typical income tax. Nationally, dividends and interest account for 15.97 percent of income. For New Hampshire, its 5 percent rate was multiplied by 15.97 percent, yielding the equivalent rate of 0.8 percent. For Tennessee, with a tax rate of 6 percent, this calculation yields an equivalent rate of 1.02 percent.

25 The local income tax rate add-ons are calculated by using a weighted average of each locality's rate. The locality's portion of the state's personal income is used as the weight. For example, in New Jersey large municipalities with populations over 200,000, can impose a payroll tax. Newark is the only city to do so currently by imposing a 1 percent tax rate. Newark's share of the state's total personal income is then used as a weight and multiplied by the 1 percent rate thereby calculating New Jersey's .09 percent add-on rate.

26 Ohio is currently phasing down its top individual income tax rate through 2010, at which time the top rate will be 5.925 percent. In 2008, Ohio's top state rate will be 6.24 percent.

27 States receive a perfect score if their top rate kicks in at a level of income that is more than one standard deviation higher than the average threshold of all the states.



first dollar of income (after accounting for the standard deduction and personal exemption). They include New Hampshire, Tennessee, Pennsylvania, Illinois, Indiana, Michigan, and Massachusetts. States with high bracket thresholds also score well and they include Maryland (\$1,005,200), California (\$1,005,083), New Jersey (\$501,000), and North Dakota, Rhode Island, and Vermont (each \$358,650). States that score poorly have arranged their multiple tax brackets so that the top rate takes effect in the middle range of income. They include Ohio (\$202,097), Arizona (\$156,602), Wisconsin (\$152,140), Minnesota (\$78,940) and Kentucky (\$77,395).

### *The Number of Brackets*

The Index converts exemptions and standard deductions to a zero bracket before tallying income tax brackets. Therefore, Pennsylvania scores the best in this variable by having only one tax bracket. States with only two brackets are Colorado, Illinois, Indiana, Massachusetts, Michigan, New Hampshire and Tennessee. On the other end of the spectrum, Missouri scores the worst in this variable by having 11 tax brackets. Other states with many brackets include Hawaii, Iowa and Ohio (all with ten brackets) and Idaho and Maryland (nine brackets).

The number of brackets listed in a state's tax statutes is not always the number used to calculate the SBTICI. From an economic perspective, standard deductions and exemptions are equivalent to an additional tax bracket with a zero tax rate. As a result, their effects on the income tax have been incorporated into existing sub-indexes.

For example, Kansas has a standard deduction of \$5,450 and a personal exemption of \$2,250 for a combined value of \$7,700. Statutorily, Kansas has a top rate on all taxable income over \$30,000 and two lower brackets that have an average width of \$15,000. But because of its deduction and exemption, Kansas's top rate actually kicks in at \$37,700 of taxable income, and it has three tax brackets below that with an average width of \$12,567.

The size of allowed standard deductions and exemptions varies considerably.<sup>28</sup> Connecticut has the largest standard deduction and exemptions (\$13,000).<sup>29</sup> Wisconsin has the second highest (\$9,490) and a number of states tie for third by

conforming to the federal system of \$8,950: Colorado, Idaho, Minnesota, New Mexico, North Dakota, Rhode Island, South Carolina and Vermont. On the other hand, Pennsylvania has no standard deduction or personal exemptions while Indiana and New Jersey allow taxpayers only a \$1,000 personal exemption.

### *The Average Width of Brackets*

Many states have several narrow tax brackets close together at the low end of the income scale including a zero bracket created by standard deductions and exemptions. Most taxpayers never notice them because they pass so quickly through those brackets and pay the top rate on most of their income. On the other hand, some states continue placing additional, progressively higher rates throughout the income spectrum, causing individuals and non-corporate businesses to alter their income-earning and tax-planning behavior. This sub-index punishes the latter group of states by measuring the average width of the brackets, rewarding those states where the average width is small, with the result that the top rate is levied on most income, acting effectively as a flat rate on all income.

The state that scores the best is Pennsylvania, since it has no separate brackets. Indiana comes in second with an average width of \$1,000. Other states with similar bracket structures include Missouri (\$1,655), Oklahoma (\$1,850), and Georgia and Illinois (\$2,000). California scores the worst with an average bracket width of \$143,561. Other low-scoring states include Maryland (\$125,650), New Jersey (\$83,500) and Vermont, Rhode Island and North Dakota (\$71,730).

## **Sub-Index #2: The Individual Income Tax Base**

States have different definitions of taxable income, and some create greater impediments to economic activity. This sub-index gives equal weight, 33 percent, to two major issues in base definition: marriage penalty and double taxation of capital income. Then it gives a 33 percent weight to an accumulation of more minor base issues.

The seven states with no individual income tax of any kind achieve perfect neutrality. Texas, however, receives a slight deduction because it

28 Some states offer tax credits in lieu of income exemptions. Rather than excluding a portion of a taxpayer's income from the income tax, tax credits reduce a taxpayer's tax liability. The result is the same: a lower income tax bill. In order to maintain consistency within the sub-index, a tax credit is converted to an equivalent income exemption.

29 In Connecticut, taxpayers receive a declining exemption and a personal tax credit. The exemption starts at \$13,000 and phases out after \$55,000 of income for single taxpayers.

does not recognize LLCs or S-Corps. Of the other 43 states, Utah, Idaho, Oregon, Indiana, Tennessee, Montana and West Virginia have the best scores. They avoid the marriage penalty and other problems with the definition of taxable income. Meanwhile, states where the tax base is found to cause an unnecessary drag on economic activity are Maryland, California, New Jersey, Rhode Island, Ohio and West Virginia.

### Marriage Penalty

A marriage penalty exists when a state's standard deduction and tax brackets for married taxpayers filing jointly are not double those for single filers. As a result, two singles (if combined) can have a lower tax bill than a married couple filing jointly with the same income. This is discriminatory and has serious business ramifications. The top-earning 20 percent of taxpayers is dominated (85 percent) by married couples. This same 20 percent also has the highest concentration of business owners (43 percent) of all income groups (Hodge 2003A, Hodge 2003B). Because of these concentrations, marriage penalties affect a large majority of taxable income. States with the largest marriage penalties include Maryland, California, New Jersey, Ohio, Rhode Island, Vermont and North Dakota.

Many states get around the marriage penalty problem by allowing married couples to file as if they were singles. While helpful in offsetting the marriage penalty, it comes at the expense of added tax complexity. Despite the complexity, the sub-index rewards states that have this provision.

### Double Taxation of Capital Income

Since several states with an individual income tax system mimic the federal income tax code, they also possess its greatest flaw—the double-taxation of capital income. Double taxation is brought about by the interaction between the corporate income tax and the individual income tax. The ultimate source of most capital income—interest, dividends and capital gains—is corporate profits. The corporate income tax reduces the level of profits that can eventually be used to generate interest or dividend payments or capital gains.<sup>30</sup> This capital income must then be declared by the receiving individual and taxed. The result is the double taxation of this capital income—first at the corporate level and again on the individual level.

All states with an individual income tax score poorly by this criterion except Tennessee and New Hampshire, which tax individuals on interest and dividends but not capital gains.

### Other Significant Issues

The index includes several individual income tax base issues that significantly affect the neutrality of state individual income tax systems.

#### *Federal Income Used as State Tax Base*

Despite the shortcomings of the federal government's definition of income, states that use it help reduce the tax compliance burden on taxpayers. Eight states do not conform to federal definitions of individual income—Alabama, Arkansas, Iowa, Mississippi, New Hampshire, New Jersey, Pennsylvania and Tennessee—and score poorly.

#### *The Alternative Minimum Tax*

The Alternative Minimum Tax (AMT) was created at the federal level in 1969 to ensure that all taxpayers paid some minimum level of taxes every year. Unfortunately, it creates a parallel tax system to the standard individual income tax code. Evidence shows that the AMT is an inefficient way to prevent tax deductions and credits from totally eliminating tax liability. As such, states that have mimicked the federal AMT put themselves at a competitive disadvantage through needless tax complexity.

Twelve states have an AMT on individuals—California, Colorado, Connecticut, Iowa, Maine, Maryland, Minnesota, Nebraska, New York, Rhode Island, West Virginia and Wisconsin—and score poorly.

#### *Deductibility of Taxes Paid*

This variable measures the extent of double taxation on income used to pay foreign and state taxes, i.e., paying a tax on a tax. States can avoid double taxation by allowing a deduction for state taxes paid to other jurisdictions.

#### *Recognition of Limited Liability Corporation and S-Corporation Status*

One important development in the federal tax system is the creation of the limited liability corporation (LLC) and the S-corporation (S-corp). LLCs and S-corps provide businesses some of the benefits of incorporation, such as limited liability, without the overhead of becoming a regular C-corporation. They also are taxed as individuals, which avoids the double-taxation problems that plague the corporate income tax system. Every state with a full individual income tax recognizes LLCs or S-corporations to at least some degree.

30 While individual capital gains taxes are not paid directly by corporations, they are a reflection of retained corporate profits.

### Indexation of the Tax Code

Indexing the tax code for inflation is critical in order to prevent de facto tax increases on the nominal increase in income due to inflation. Put simply, this “inflation tax” results in higher tax burdens on taxpayers, usually without their knowledge or consent. Three areas of the individual income tax are commonly indexed for inflation: the standard deduction, personal exemptions and tax brackets.

Fourteen states index all three,<sup>31</sup> ten states do not index at all<sup>32</sup> and nineteen states and the District of Columbia index at least one of the three.

## Sales Tax Index

The type of sales tax familiar to all taxpayers is a tax levied on the purchase price of a good or service at the point of sale. This point-of-sale tax can hurt the business tax climate because as the sales tax rate climbs, customers either make fewer purchases or seek out low-tax alternatives. As a result, business is lost to lower-tax locations, causing lost profits, lost jobs and lost tax revenue.<sup>33</sup> The effect of differential sales tax rates between states or localities is apparent when a traveler crosses the state line from a high-tax state to a neighboring low-tax state. Typically, a vast expanse of shopping malls has sprung up along the border in the low-tax jurisdiction.

On the positive side, sales taxes levied on goods and services at the point of sale to the end user have at least two virtues. They are “transparent,” i.e., the tax is never confused with the price of goods by customers, and since they are levied at the point of sale, they are less likely to cause economic distortions than taxes levied at some intermediate stage of production.

More detrimental to the business climate are sales taxes levied on business-to-business transactions. When a business must pay sales taxes on manufacturing equipment and raw materials, then that tax becomes part of the price of whatever the business makes with that equipment and those materials. Of course, it must then collect sales tax on its own products, with the result that a tax is

being charged on a tax. So-called “tax pyramiding” invariably results in some industries being taxed more heavily than others, which causes economic distortions.

Consider the following quote from David Brunori, contributing editor of *State Tax Notes*:

A graduate student wrote me recently and asked what I thought was the most egregious flaw embedded in the state tax system. I told her that I thought there were about 100 flaws that could vie for the top spot. Here is one: the sales tax on business purchases. Everyone who has ever studied the issue will tell you that the sales tax should not be imposed on business purchases. That is, when a business purchases a product or service, it should not pay tax on the purchase. There is near unanimity among public finance scholars on the issue. The sales tax is supposed to be imposed on the final consumer. Taxing business purchases causes the tax to be passed on to consumers without their knowledge. There is nothing efficient or fair about that. But business purchases are taxed widely in every state with a sales tax.

Some studies have estimated that business taxes make up nearly 50 percent of total sales tax revenue. Why? Two reasons. First, because business sales taxes raise so much money that the states cannot repeal them. The states would have to either raise other taxes or cut services. Second, many politicians think it is only fair that “businesses” pay taxes because individuals pay them. That ridiculous belief is unfortunately shared by many state legislators; it’s usually espoused by liberals who don’t understand that businesses aren’t the ones who pay taxes. People do. Every time a business pays sales tax on a purchase, people are burdened. They just don’t know it.<sup>34</sup>

### MAINE

Maine had no significant tax changes for FY 2009, and it remained in 40<sup>th</sup> place on the overall index. This fall, Maine’s governor and legislative leaders have discussed the possibility of cutting Maine’s income tax rate, one of the nation’s highest at 8.5%. Unlike most states with high top tax rates, Maine’s 8.5% rate kicks in at under \$20,000 of taxable income, applying a high marginal rate to much more than just the “rich.” Maine’s income tax compares particularly unfavorably to its nearest competitors: Massachusetts, which has a flat, 5.3% income tax; and New Hampshire, which has no general tax on personal income.

31 States with a single rate system that do not have any brackets to adjust for inflation are treated as if they were indexation states. These states include Colorado, Illinois, Indiana, Massachusetts, Michigan, New Hampshire, Tennessee and Utah.

32 This variable only looks at states that have statutory automatic provisions to index the standard deduction, personal exemption or tax brackets to inflation. This does not reflect recent or ongoing legislative activity whose end result may be to adjust these provisions for the effects of inflation.

33 Of course, states try to limit sales tax competition by levying a use tax on goods purchased out of state and brought into the state. Enforcement of use tax obligations against consumers is nearly impossible, especially after the Supreme Court’s decision in *Quill v. Heitkamp*, 504 U.S. 298 (1992), where the Court ruled that vendors without physical presence (offices, employees, etc.) in a state could not be forced to collect use tax. The Streamlined Sales Tax Project is a current effort of state revenue commissioners and multistate businesses to harmonize state sales and use tax bases such that Congress could be justified in overturning the *Quill* decision.

34 David Brunori, “An Odd Admission of Gambling,” *State Tax Notes*, Jan. 30, 2005, p. 332-339.

The negative impact of sales taxes is well documented in the economic literature and through anecdotal evidence. For example, Bartik

(1989) found that high sales taxes, especially sales taxes levied on equipment, had a negative effect on small business start-ups. Moreover, companies

**Table 5**  
*Sales Tax Index, 2006 – 2009*

State	FY 2009 State Business Tax Climate Index		FY 2008 State Business Tax Climate Index		Change from 2007 to 2008		FY 2007 State Business Tax Climate Index		FY 2006 State Business Tax Climate Index	
	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank
U.S.	5.00	–	5.00	–	5.00	–	5.00	–	5.00	–
Alabama	4.90	33	5.00	28	–0.10	–5	5.19	24	5.18	24
Alaska	9.29	4	9.28	3	0.02	–1	9.29	3	9.63	1
Arizona	4.19	45	4.15	45	0.03	0	4.26	43	4.32	43
Arkansas	4.72	35	4.61	37	0.11	2	4.63	37	4.56	38
California	4.34	43	4.37	41	–0.03	–2	4.30	42	4.42	42
Colorado	5.68	12	5.70	14	–0.01	2	5.40	19	5.35	21
Connecticut	5.18	25	5.13	25	0.05	0	5.01	31	4.93	31
Delaware	9.49	2	9.55	2	–0.06	0	9.53	2	9.53	3
Florida	5.29	21	5.22	23	0.07	2	5.20	23	5.45	18
Georgia	5.48	16	5.44	17	0.04	1	5.54	15	5.55	16
Hawaii	5.04	29	4.97	31	0.07	2	5.31	21	5.53	17
Idaho	4.98	32	4.94	33	0.04	1	4.87	32	4.77	34
Illinois	4.63	39	4.79	34	–0.16	–5	4.79	35	4.88	33
Indiana	5.40	19	5.97	11	–0.57	–8	5.85	12	5.91	12
Iowa	5.13	26	5.36	18	–0.23	–8	5.45	18	5.41	19
Kansas	5.43	17	5.24	22	0.19	5	5.09	29	4.92	32
Kentucky	6.15	7	6.15	9	0.00	2	5.99	11	5.99	10
Louisiana	4.12	46	4.12	46	0.00	0	4.00	46	3.97	46
Maine	6.11	8	6.02	10	0.08	2	6.01	10	5.98	11
Maryland	5.95	10	6.62	7	–0.67	–3	6.43	7	6.34	7
Massachusetts	6.03	9	6.18	8	–0.16	–1	6.15	8	6.13	8
Michigan	5.92	11	5.84	12	0.08	1	5.82	13	5.78	13
Minnesota	4.59	40	4.55	40	0.04	0	4.59	38	4.58	37
Mississippi	4.83	34	4.77	35	0.06	1	4.64	36	4.61	36
Missouri	5.25	22	5.25	21	–0.01	–1	5.11	27	5.09	28
Montana	9.30	3	9.26	4	0.05	1	9.23	5	9.21	5
Nebraska	4.40	42	4.23	43	0.17	1	4.10	45	4.06	45
Nevada	4.21	44	4.20	44	0.01	0	4.21	44	4.25	44
New Hampshire	9.58	1	9.56	1	0.03	0	9.56	1	9.61	2
New Jersey	4.51	41	4.30	42	0.21	1	5.15	26	5.13	26
New Mexico	4.09	47	4.06	47	0.03	0	3.95	47	3.95	47
New York	2.99	49	3.11	49	–0.12	0	3.27	49	3.21	49
North Carolina	4.64	38	4.58	39	0.06	1	4.43	41	4.43	41
North Dakota	5.11	27	5.04	27	0.07	0	5.04	30	5.02	29
Ohio	4.68	36	4.72	36	–0.04	0	4.52	40	4.43	40
Oklahoma	5.03	31	4.98	30	0.05	–1	4.84	33	4.96	30
Oregon	9.28	5	9.25	5	0.04	0	9.24	4	9.24	4
Pennsylvania	5.19	24	5.10	26	0.10	2	5.23	22	5.15	25
Rhode Island	5.04	30	4.94	32	0.09	2	4.79	34	4.68	35
South Carolina	5.62	13	5.61	15	0.02	2	6.09	9	6.11	9
South Dakota	4.66	37	4.60	38	0.06	1	4.57	39	4.54	39
Tennessee	3.56	48	3.51	48	0.05	0	3.55	48	3.52	48
Texas	5.06	28	4.99	29	0.07	1	5.18	25	5.13	27
Utah	5.21	23	5.14	24	0.07	1	5.10	28	5.30	22
Vermont	5.55	15	5.48	16	0.06	1	5.47	17	5.64	15
Virginia	6.85	6	6.78	6	0.06	0	6.62	6	6.57	6
Washington	2.90	50	2.87	50	0.03	0	2.80	50	2.90	50
West Virginia	5.34	20	5.26	20	0.07	0	5.51	16	5.41	20
Wisconsin	5.42	18	5.35	19	0.08	1	5.33	20	5.30	23
Wyoming	5.62	14	5.76	13	–0.14	–1	5.60	14	5.65	14
D.C.	4.64	–	4.58	–	0.06	–	4.41	–	4.35	–

**Note:** The higher the score the better, the more favorable a state's tax system is for business. All scores are for fiscal years.

**Source:** Tax Foundation



have been known to avoid locating factories or facilities in certain states because the factory's machinery would be subject to the state's sales tax.<sup>35</sup>

To understand how business-to-business sales taxes can distort the market, suppose a sales tax were levied on the sale of flour to a bakery. The bakery is not the end-user because the flour will be baked into bread and sold to consumers. Economic theory is not clear as to which party will ultimately bear the burden of the tax. The tax could be "passed forward" onto the customer or "passed backward" onto the bakery.<sup>36</sup> Where the tax burden falls depends on how sensitive the demand for bread is to price changes. If customers tend not to change their bread-buying habits when the price rises, then the tax can be fully passed forward onto consumers. However, if the consumer reacts to higher prices by buying less, then the tax will have to be absorbed by the bakery as an added cost of doing business.

The hypothetical sales tax on all flour sales would distort the market because different businesses that use flour have customers with varying price sensitivity. Suppose the bakery is able to pass the entire tax on flour forward to the consumer, but the pizza shop down the street cannot. The owners of the pizza shop would face a higher cost structure and profits would drop. Since profits are the market signal for opportunity, the tax would tilt the market away from pizza-making. Fewer entrepreneurs would enter the pizza business, and existing businesses would hire fewer people. In both cases, the sales tax charged to purchasers of bread and pizza would be partly a tax on a tax because the tax on flour would be built into the price. Economists call this tax pyramiding.

Besley and Rosen (1998) found that for many products, the after-tax price of the good increased

by the same amount as the tax itself. That means a sales tax increase was passed along to consumers on a one-for-one basis. For other goods, however, they found that the price of the good rose by twice the amount of the tax, meaning that the tax increase translates into an even larger burden for consumers than is typically thought.

The Sales Tax Index is weighted so that it makes up 22.21 percent of a state's total score on the SBTCL. See Tables 15, 16 and 17 in the appendix for details of each state's sales tax system. It is comprised of two equally weighted sub-indexes devoted to the sales tax rate and the tax base. The rate sub-index is calculated using two criteria: the state-level rate and the combined state-local rate. States will score well if they either do without a sales tax or if the combined state and local sales tax rate is low. The ideal base for sales taxation is all goods and services at the point of sale to the end user.<sup>37</sup>

States that create the most tax pyramiding and economic distortion, and therefore score the worst, are states that levy a sales tax that generally allows no exclusions for business inputs.<sup>38</sup> Hawaii, New Mexico,<sup>39</sup> Washington and South Dakota<sup>40</sup> are examples of states that tax many business inputs.

Selective sales taxes, or excise taxes, are taxes levied on specific goods. Goods that are typically perceived as vices, such as cigarettes and alcohol, and those that are not subject to large changes in demand when their prices increase, such as gasoline, are the most likely to be subject to excise taxes. The Sales Tax Index takes into account the excise tax rates each state levies.

The five states without a state sales tax—Alaska, Delaware, New Hampshire, Oregon, and Montana—achieve the best scores on this index. For states with a sales tax, Virginia has the best score because it does a good job of avoiding tax

35 In early 1993, Intel Corporation was considering California, New Mexico and four other states as the site of a new billion dollar factory. California was the only one of the six states that levied its sales tax on machinery and equipment, a tax that would have cost Intel roughly \$80 million. As Intel's Bob Perlman put it in testimony before a committee of the California state legislature, "There are two ways California's not going to get the \$80 million, with the factory or without it." California would not repeal the tax on machinery and equipment; New Mexico got the plant.

36 See Besley and Rosen, *op. cit.*

37 In some cases, transactions that appear to be business-to-business turn out to be business-to-consumer. For example, a hobby farmer needs many of the same business inputs as a commercial farmer. Thus, the hobby farmer is able to take advantage of the same sales tax exclusions as the commercial farmer. Such cases are rare, however, and therefore are not accounted for in this sub-index.

38 Sales taxes that are levied on stages of production are known as value-added taxes (VAT) and are popular internationally because they attempt to neutralize the negative economic impact of tax pyramiding. The VAT has never gained wide acceptance in the U.S., and only one state (Michigan) has even attempted a VAT-like tax.

39 New Mexico's score is improved by its business exclusion for farmers and ranchers.

40 South Dakota has a gross receipts tax base, but businesses "have the right" to pass the tax onto the consumer via a complex refund formula. Depending on how many businesses bother to exercise their "right" to pass the tax onto consumers, this could be called either a sales tax or a gross receipts tax. States that use the term "sales tax" may actually have a gross receipts tax and vice-versa. This makes identification difficult, but the structure of the index is designed to reflect the level of tax pyramiding within a state's sales tax.

pyramiding and maintains low excise tax rates. Other states that score well include Kentucky, Maine, Massachusetts and Maryland. They tend to have average or below-average tax rates, exempt most business input items from sales tax, and maintain low or moderate excise taxes.

---

*New York and Louisiana have the highest average local option sales taxes (4.25 and 4.16 percent respectively), and in both states the average local option sales tax is higher than the state sales tax rate of 4 percent. Other states with high local option sales taxes include Missouri (3.22 percent), Alabama (3.15 percent), Georgia (2.76 percent) and North Carolina (2.58 percent).*

---

At the other end of the spectrum, Washington levies its sales tax on most business inputs—such as services, manufacturing, and leases—and maintains relatively high excise taxes. Joining Washington at the bottom are New York, Tennessee, New Mexico and Louisiana. Tennessee has the highest combined state and local rate of 9.36 percent. These states levy high sales tax rates that apply to most or all business input items. See Table 5 for state rankings.

### Sub-Index #1: Sales Tax Rate

The tax rate itself is important, and a state with a high sales tax rate reduces demand for in-state retail sales. Consumers will turn more frequently to out-of-state, catalog, or internet purchases, leaving less business activity in state. This sub-index measures the highest possible sales tax rate applicable to in-state retail shopping and taxable business-to-business transactions. Four states—Delaware, Montana, New Hampshire and Oregon—do not have a general state sales tax and thus are given a rate of zero. Alaska is generally counted among states with no sales tax since it does not levy a statewide sales tax. However, Alaska localities are allowed to levy sales taxes, and

the weighted average of county and municipal taxes is 0.86 percent.

The SBTCI measures the state and local sales tax rate in each state. A combined rate is computed by adding the general state rate to the weighted average of the county and municipal rates.

### State Sales Tax Rate

Of the states with a statewide sales tax, Colorado's 2.9 percent rate is lowest. Eight states have a 4 percent state-level sales tax: Alabama, Georgia, Hawaii, Louisiana, New York, South Dakota, Virginia<sup>41</sup> and Wyoming.

The states with the worst score in this sub-index are Indiana, Mississippi, New Jersey, Rhode Island and Tennessee with their 7 percent statewide rates. Other states with high statewide rates include Nevada, Washington and Minnesota (6.5 percent) and Texas, Illinois and California (6.25 percent).

### Local Option Sales Tax Rates

State-level sales taxes are only part of the story. Thirty-three states authorize the use of local option sales taxes at the county and/or municipal level.<sup>42</sup> Local jurisdictions in Colorado, for example, add 1.85 percent in local sales taxes to the state's 2.9 percent state-level rate, bringing the total sales tax rate to 4.75 percent. This may be an understatement in some localities with much higher local add-ons, but by using the weighted average for each state's local rates, the index makes the states comparable. In some states, the local option sales tax significantly increases the tax rate faced by consumers.

New York and Louisiana have the highest average local option sales taxes (4.25 and 4.16 percent respectively), and in both states the average local option sales tax is higher than the state sales tax rate of 4 percent. Other states with high local option sales taxes include Missouri (3.22 percent), Alabama (3.15 percent), Georgia (2.76 percent) and North Carolina (2.58 percent).

The sub-index adds the state and local taxes together and grades states on the combined rate. States with the highest combined rates are Tennessee (9.36 percent), Washington (8.62 percent), New York (8.25 percent), Louisiana (8.16 percent) and California (7.96 percent). At the low end are Hawaii (4.38 percent), Colorado (4.75 percent), and Maine, Massachusetts and Virginia (5.0 percent).

41 On top of its 4% state rate, Virginia levies a uniform and standard 1 percent "local option" tax for the entire state.

42 The local option sales tax rate is calculated on a weighted average basis. Each county rate is weighted by its percentage of total state personal income.

Another difficulty businesses face with some local option sales taxes is that not only do rates differ, but some states also allow localities to define their own sales tax base, multiplying complexity for businesses and consumers. These states are Colorado, Idaho and New York.

## Sub-Index #2: Sales Tax Base

The sales tax base sub-index is computed according to three features of each state's sales tax: (1) whether the base includes a variety of business-to-business transactions such as agricultural products, services, machinery, computer software, and leased or rented items; (2) whether the base includes goods and services typically purchased by consumers; and (3) the excise tax rate on products such as gasoline, diesel fuel, tobacco, spirits and beer.

The top five states on this sub-index are those without a general sales tax—New Hampshire, Delaware, Montana, Alaska and Oregon. None receives a perfect score because they all levy gasoline, diesel, tobacco and beer excise taxes. For the states that do have a general sales tax, Missouri, Virginia, South Carolina, Kentucky and Indiana have the highest scores. These states avoid the problems of tax pyramiding and have low excise tax rates.

On the other hand, the states with the worst scores on the base sub-index are Hawaii, New Mexico, Washington, South Dakota and Nebraska. Their tax systems are hampering economic growth due to the inclusion of too many business inputs, the exclusion of too many consumer goods and services, and/or excessive rates of excise taxation.

The extent of business-to-business sales taxation is measured by tallying exemptions for six categories of intermediate goods and services. The categories of business purchases tallied by this sub-index are: agricultural inputs, service inputs, manufacturing and machinery inputs, computer and software inputs, leasing and rental inputs, and pollution control equipment. Second, exemptions from the sales tax base of groceries and gasoline are included since the best sales tax system is one that offers the fewest exemptions for consumer products and services, even for staples such as groceries and gas. Finally, because excise taxes single out products for extra taxes, essentially the mirror image of a tax exemption, they are tallied in this sub-index as well.

### Business Inputs

These variables are often inputs to other business operations. For example, a manufacturing firm

will count the cost of transporting its final goods to retailers as a significant cost of doing business. Most firms, small and large alike, hire accountants, lawyers, and other professional service firms. If these services are taxed, then it is more expensive for every business to operate.

Note that these inputs should only be exempt from sales tax if they are truly inputs into the production process. If they are consumed by an end user, they are properly includable in the state's sales tax base.

#### *Agricultural Inputs*

- Insecticides and pesticides
- Fertilizer, seed and feed
- Seedlings, plants and shoots

#### *Service Inputs*

- Cleaning services
- Transportation services
- Repair services
- Professional/personal services
- General treatment

#### *Manufacturing and Machinery Inputs*

- Manufacturing machinery
- Utilities
- Farm machinery
- Raw material
- Office equipment

#### *Computer and Software Inputs*

- Custom software
- Modified canned software
- Downloaded software

#### *Leasing and Rental Inputs*

- Motor vehicles
- Rooms and lodging
- All other tangible personal property

#### *Pollution Control Equipment*

- Air pollution control equipment
- Water pollution control equipment

## Consumer Goods and Services

State sales tax bases should include all goods and services purchased by the end users of those products. Exempting any goods or services narrows the tax base, drives up the sales tax rate, and introduces unnecessary distortion into the market.

### *Gasoline*

Purchases of gasoline should be included in the sales tax base, even though every state subjects

gasoline to a separate excise levy at the distributor stage of production. Ideally, the excise tax can be viewed as a user fee that funds road construction, and where this is the case, no damaging tax pyramiding is caused by levying both an excise and a general sales tax on gasoline. There is no economic reason to exclude gasoline from the sales tax base since the sales tax is intended to apply broadly to all consumption. Thus, the Index gives a better score to states that include gasoline in the sales tax base.

---

*Since gasoline represents a large input for most businesses, states that levy higher rates have a less competitive business tax climate. States with the highest gasoline taxes are Washington (37.5 cents), New York and Florida (33.2 cents), Wisconsin (32.9 cents), Nevada and Hawaii (32.6 cents), and Pennsylvania (32.3 cents). States with the lowest gasoline taxes are Georgia (7.5 cents), Alaska (8.0 cents), Wyoming (14 cents) and New Jersey (14.5 cents).*

---

Four states fully include gasoline in their sales tax base: California, Illinois, Indiana, and Michigan. Connecticut, Georgia and New York get partial credit for applying an ad valorem tax to gasoline sales, but at a different rate than for the general sales tax.

#### **Groceries**

A principled approach to sales tax policy calls for all end-user goods to be included in the tax base, to keep the base broad, rates low, and prevent distortions in the marketplace. Should groceries be the exception?

Many state officials will say that they exempt groceries in order to make the sales tax system easier on low-income people. In reality, exempting groceries from the sales tax mostly benefits grocers, not the poor, although even grocers have occasion to complain because the maintenance of complex, ever-changing lists of exempt and non-exempt products constitutes an administrative burden for all concerned. Most importantly,

though, widespread availability of public assistance for the purchase of groceries—from the Women, Infants and Children program or the food-stamp program—makes the argument for such exemptions unpersuasive.

---

*A principled approach to sales tax policy calls for all end-user goods to be included in the tax base, to keep the base broad, rates low, and prevent distortions in the marketplace.*

---

Fifteen states include or partially include groceries in their sales tax base. Tennessee, Utah, West Virginia, Illinois, Missouri, Arkansas and Virginia partially include groceries, while Alabama, Hawaii, Idaho, Kansas, Mississippi, Oklahoma, South Carolina and South Dakota wholly include groceries in the sales tax base.

#### **Excise Taxes**

Excise taxes are single-product sales taxes. Many of them are intended to reduce consumption of the product bearing the tax. Others, like the gasoline tax, are often used to fund specific projects like road construction. The sub-index tallies:

- Gasoline excise tax
- Diesel excise tax
- Tobacco excise tax
- Beer excise tax
- Spirits excise tax

Gasoline and diesel excise taxes (levied on a per gallon basis) are usually levied on the benefit principle as a means to pay for road construction and maintenance. Since gasoline represents a large input for most businesses, states that levy higher rates have a less competitive business tax climate. States with the highest gasoline taxes are Washington (37.5 cents), New York and Florida (33.2 cents), Wisconsin (32.9 cents), Nevada and Hawaii (32.6 cents), and Pennsylvania (32.3 cents). States with the lowest gasoline taxes are Georgia (7.5 cents), Alaska (8.0 cents), Wyoming (14 cents) and New Jersey (14.5 cents). States with the highest diesel tax are Connecticut (43.4 cents), Pennsylvania (39.2 cents), and Washington (37.5 cents), while states with the lowest diesel tax are Georgia (7.5 cents), Alaska (8.0 cents), and Oklahoma and Wyoming (14 cents).



Tobacco, spirits and beer excise taxes are mostly problematic because they discourage in-state consumption and encourage consumers to seek lower prices in neighboring jurisdictions (Moody and Warcholik, 2004). This impacts a wide swath of retail outlets, such as convenience stores, that move large volumes of tobacco and beer products. The problem is exacerbated for those retailers located near the border of states with lower excise taxes as consumers move their shopping out of state—referred to as cross-border shopping.

---

*One of the worst aspects of the UI tax system is that financially troubled businesses, where layoffs may be a matter of survival, actually pay higher marginal rates as they are forced into higher tax rate schedules. In the academic literature, this has long been called the “shut-down effect” of UI taxes: failing businesses face climbing UI taxes, with the result that they fail sooner.*

---

In addition to cross-border shopping, there is also the growing problem of cross-border smuggling of products from states that levy low excise taxes on tobacco into states that levy high excise taxes on tobacco. This both increases criminal activity and reduces taxable sales by legitimate retailers (Fleenor 1998).

States with the highest tobacco taxes per pack of 20 cigarettes are New York (\$2.75), New Jersey (\$2.575), Massachusetts (\$2.51), and Rhode Island (\$2.46), while states with the lowest tobacco taxes are South Carolina (7 cents), Missouri (17 cents) and Mississippi (18 cents). States with the highest beer taxes on a per gallon basis are Alaska (\$1.07), Georgia (\$1.01), and Hawaii (93 cents), while states with the lowest beer taxes are Wyoming (2 cents), Missouri (6 cents) and Wisconsin (6 cents). States with the highest spirits taxes per gallon are Washington (\$21.30), Oregon (\$18.52) and Alabama (\$14.78).

## Unemployment Insurance Tax Index

The fourth index is the Unemployment Insurance Tax index. Unemployment Insurance (UI) taxes are paid by employers into the UI program to finance benefits for workers recently unemployed. Unlike the other major taxes assessed in the State Business Tax Climate Index, UI taxes are much less well known, every state has one, and there are no perfect or even nearly perfect UI tax systems. All are complex, variable-rate systems that impose different rates on different industries and different bases depending upon such factors as the health of the state's UI trust fund.

One of the worst aspects of the UI tax system is that financially troubled businesses, where layoffs may be a matter of survival, actually pay higher marginal rates as they are forced into higher tax rate schedules. In the academic literature, this has long been called the “shut-down effect” of UI taxes: failing businesses face climbing UI taxes, with the result that they fail sooner.

The Unemployment Insurance Tax Index consists of two sub-indexes, one that measures each state's rate structure and one that focuses on the tax base. Each is weighted to represent half of the total index score.

---

*The states with the worst UI taxes are Rhode Island, Massachusetts, Kentucky, Alaska and Michigan. These states tend to have rate structures with high minimum and maximum rates and wage bases above the federal level. Moreover, they have more complicated experience formulas and charging methods, and they have added benefits and surtaxes to their systems.*

---

Overall, the states with the least damaging UI taxes are Oklahoma, Arizona, Florida, Missouri and Mississippi. Comparatively speaking, these states have rate structures with lower minimum

and maximum rates and a wage base at the federal level. In addition, they have simpler experience formulas and charging methods, and they have

not complicated their systems with benefit additions and surtaxes.

On the other hand, the states with the worst UI taxes are Rhode Island, Massachusetts,

**Table 6**  
*Unemployment Insurance Tax Index, 2006 – 2009*

State	FY 2009 State Business Tax Climate Index		FY 2008 State Business Tax Climate Index		Change from 2008 to 2009		FY 2007 State Business Tax Climate Index		FY 2006 State Business Tax Climate Index	
	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank
U.S.	5.00	—	5.00	—	5.00	—	5.00	—	5.00	—
Alabama	5.57	14	5.60	12	-0.03	-2	6.06	8	6.23	4
Alaska	3.78	47	3.30	48	0.48	1	3.83	45	3.91	43
Arizona	6.41	2	6.42	2	-0.01	0	5.96	10	5.91	12
Arkansas	5.08	23	5.09	25	-0.01	2	4.49	35	4.05	41
California	5.47	16	5.49	15	-0.02	-1	5.50	18	5.50	20
Colorado	5.32	19	5.22	19	0.10	0	5.20	23	5.27	21
Connecticut	5.20	21	5.27	18	-0.07	-3	5.65	16	5.01	26
Delaware	5.88	7	5.99	7	-0.11	0	5.99	9	5.95	11
Florida	6.20	3	6.22	3	-0.01	0	6.49	3	6.62	1
Georgia	5.20	20	5.21	21	-0.01	1	4.69	32	4.64	32
Hawaii	5.66	11	5.19	22	0.47	11	5.18	24	5.24	22
Idaho	4.01	45	4.03	44	-0.02	-1	3.49	47	3.68	46
Illinois	4.33	43	4.29	42	0.04	-1	4.47	36	4.34	37
Indiana	5.62	13	5.64	10	-0.02	-3	5.55	17	6.05	7
Iowa	4.66	35	4.70	37	-0.04	2	5.01	27	4.96	28
Kansas	5.85	8	5.74	9	0.11	1	5.78	12	5.72	15
Kentucky	3.52	48	3.59	47	-0.07	-1	3.35	48	3.35	48
Louisiana	5.76	10	5.79	8	-0.03	-2	5.95	11	6.01	9
Maine	4.43	40	4.46	40	-0.03	0	4.34	40	3.98	42
Maryland	4.79	31	4.83	30	-0.04	-1	4.76	30	5.63	17
Massachusetts	3.04	49	3.17	49	-0.13	0	2.75	49	2.76	49
Michigan	4.00	46	4.01	45	-0.02	-1	4.22	42	4.18	40
Minnesota	4.52	38	4.58	39	-0.06	1	4.35	39	4.55	35
Mississippi	6.02	5	6.09	5	-0.07	0	6.63	2	6.58	2
Missouri	6.16	4	6.13	4	0.02	0	6.09	7	6.02	8
Montana	5.37	18	5.22	20	0.14	2	5.22	21	5.16	24
Nebraska	5.64	12	5.41	17	0.23	5	5.09	26	5.73	14
Nevada	4.37	42	4.44	41	-0.07	-1	4.29	41	4.26	38
New Hampshire	4.51	39	4.65	38	-0.14	-1	3.95	44	3.91	44
New Jersey	5.07	24	5.15	23	-0.07	-1	5.13	25	4.99	27
New Mexico	5.46	17	5.60	13	-0.14	-4	5.66	15	5.60	18
New York	4.03	44	3.85	46	0.18	2	3.62	46	3.62	47
North Carolina	6.00	6	6.04	6	-0.04	0	6.19	4	6.13	5
North Dakota	4.66	34	4.87	29	-0.21	-5	4.37	38	4.46	36
Ohio	5.52	15	5.64	11	-0.12	-4	5.34	19	5.88	13
Oklahoma	6.67	1	6.59	1	0.08	0	6.74	1	6.43	3
Oregon	4.82	30	4.77	32	0.05	2	4.89	29	4.77	30
Pennsylvania	5.02	26	5.13	24	-0.11	-2	5.76	13	5.71	16
Rhode Island	2.58	50	2.62	50	-0.04	0	2.18	50	2.33	50
South Carolina	4.40	41	4.14	43	0.26	2	3.95	43	3.87	45
South Dakota	4.59	37	4.77	33	-0.19	-4	4.75	31	4.70	31
Tennessee	4.77	32	4.83	31	-0.06	-1	4.66	33	4.60	33
Texas	5.78	9	5.54	14	0.25	5	6.09	6	6.06	6
Utah	4.94	27	4.93	27	0.02	0	5.25	20	5.21	23
Vermont	5.18	22	5.48	16	-0.30	-6	6.09	5	5.99	10
Virginia	4.84	29	4.91	28	-0.07	-1	5.21	22	5.16	25
Washington	4.63	36	4.74	36	-0.11	0	4.45	37	4.24	39
West Virginia	4.75	33	4.76	35	-0.01	2	4.66	34	4.57	34
Wisconsin	5.06	25	5.07	26	-0.01	1	5.00	28	4.95	29
Wyoming	4.86	28	4.77	34	0.09	6	5.67	14	5.53	19
D.C.	5.02	—	5.04	—	-0.02	—	5.00	—	4.96	—

**Note:** The higher the score, the more favorable a state's tax system is for business. All scores are for fiscal years.

**Source:** Tax Foundation

Kentucky, Alaska and Michigan. These states tend to have rate structures with high minimum and maximum rates and wage bases above the federal level. Moreover, they have more complicated experience formulas and charging methods, and they have added benefits and surtaxes to their systems (see Table 6). The Unemployment Insurance Tax Index is weighted 12.16 percent of a state's final SBTCI score. See Tables 18, 19 and 20 in the appendix for details of each state's system.

## Sub-Index #1: Unemployment Insurance Tax Rate

UI tax rates in each state are based on a schedule ranging from a minimum rate to a maximum rate. The schedule for any particular business is dependent upon the business's experience rating. The rate is then applied to a taxable wage base (a predetermined fraction of an employee's wage) to determine UI tax liability.

Overall, the states with the best score on this sub-index are Arizona, Nebraska, Florida, Georgia, and Virginia. Generally, these states have low minimum and maximum tax rates on each schedule and a wage base at or near the federal level. The states with the worst scores are Massachusetts, Rhode Island, Minnesota, Kentucky and North Dakota.

The sub-index gives equal weight to two factors: the actual rates levied in the most recent year, and the statutory rate schedules that can potentially be implemented at any time depending on the state of the economy and the UI fund.

### Tax Rates in the Most Recent Year

#### *Minimum Tax Rate*

States with the best scores in this variable are Colorado, Hawaii, Kansas, Iowa, Missouri, Montana, Nebraska, North Carolina, South Dakota and Wisconsin, all of which had a minimum rate of zero. On the other end of the spectrum, the highest rates and, thus, the worst scores are found in Rhode Island (1.69 percent), West Virginia (1.5 percent), California (1.3 percent), Massachusetts (1.12 percent) and Indiana (1.1 percent).

#### *Maximum Tax Rate*

Seventeen states receive the highest scores in this variable because they have a relatively low tax rate

of 5.4 percent.<sup>43</sup> The states are: Alaska, Arizona, California, Colorado, Connecticut, Florida, Georgia, Hawaii, Idaho, Maine, Mississippi, Nebraska, Nevada, New Jersey, New Mexico, Oregon and South Carolina. States with the highest rates and, thus, the worst scores on this variable are Massachusetts (10.96 percent), Michigan (10.3 percent), Tennessee and Arkansas (10.0 percent), and North Dakota (9.86 percent).

#### *Taxable Wage Base*

Eight states receive the best score in this variable with a taxable wage base of \$7,000—in line with the federal taxable wage base. The states with the highest taxable bases and, thus, the worst scores on this variable are Washington (\$34,000), Idaho (\$32,200), Alaska (\$31,300), Oregon (\$30,200) and New Jersey (\$27,700).

States with the best UI tax rate systems are Arizona, Florida, Georgia, Nebraska and Colorado. They have low minimum and maximum rates and a low taxable wage base. The states with the worst scores are Rhode Island, Massachusetts, Minnesota, Alaska and North Dakota. These states generally have high minimum and maximum rates and a high taxable wage base.

### Potential Rates

Due to business and seasonal cycles, all the businesses in each state will probably be forced to change UI tax rate schedules at some point each year. When UI trust funds are flush, businesses will trend toward the most favorable rate schedules; however, when UI trust funds are low, businesses will trend toward the least favorable rate schedules. Not only are the rates themselves important from a neutrality perspective, but states with a large differential between the minimum and maximum rates are less neutral than states with smaller differentials.

### Most Favorable Tax Rate Schedule

#### *Minimum Tax Rate Schedule*

Twenty-one states receive the best score in this variable with a minimum tax rate of zero, which they levy when unemployment is low and the UI fund is flush. The states with the highest minimum tax rates and thus the worst scores are Massachusetts (0.8 percent), Rhode Island (0.6 percent), South Carolina (0.54 percent) and Oregon and Connecticut (0.5 percent).

<sup>43</sup> The federal government levies its own UI tax called the Federal Unemployment Tax Act (FUTA) with a rate of 6.2 percent on wages up to \$7,000. However, the federal government provides a tax credit worth up to 5.4 percent of the wage base. As a result, the lowest state maximum rate is 5.4 percent in order to maximize the use of the federal tax credit. Therefore, the effective federal rate is a much lower 0.8 percent and is used predominantly to offset the administrative costs associated with oversight of the unemployment trust fund.

### *Maximum Tax Rate Schedule*

Twenty-three states receive the best score in this variable with a comparatively low maximum tax rate of 5.4 percent. The states with the highest maximum tax rates and thus the worst maximum tax scores are Michigan (10.3 percent), Wyoming and Tennessee (10.0 percent) and Kentucky, Minnesota and Utah (9.0 percent).

### **Least Favorable Tax Rate Schedule**

#### *Minimum Tax Rate Schedule*

Four states receive the best score in this variable with a minimum tax rate of zero percent: Iowa, Missouri, Nebraska and North Carolina. The states with the highest minimum tax rates and, thus, the worst minimum tax scores are New Mexico (2.7 percent), Hawaii (2.4 percent), Oregon and Maryland (2.2 percent) and Rhode Island and Connecticut (1.9 percent).

#### *Maximum Tax Rate Schedule*

Ten states receive the best score in this variable with a comparatively low maximum tax rate of 5.4 percent. The states with the highest maximum tax rates and, thus, the worst maximum tax scores are Massachusetts (15.4 percent), Maryland (13.5 percent), Arkansas (10.8 percent) and Michigan (10.3 percent).

Overall, the states with the best scores on their potential statutory UI tax rates are Nebraska, Washington, Arizona, North Carolina and Virginia. Nebraska gets a perfect 10, with all of their potential rates at the lowest rates. The other top states follow the same pattern with slight deviations. The states with the worst scores are Massachusetts, Maryland, Rhode Island, Kentucky and South Dakota. Many of these states have double-digit maximum tax rates.

## **Sub-Index #2: Unemployment Insurance Tax Base**

The UIT base sub-index scores states on how they determine which businesses should pay the UI tax and how much, as well as other UI-related taxes for which businesses may also be liable.

The states that receive the best scores on this sub-index are Oklahoma, Delaware, Ohio, Vermont, Missouri and Arizona. In general, these states have relatively simple experience formulas, they exclude more factors from the charging method, and they enforce fewer surtaxes.

States that receive the worst scores are Rhode Island, Alaska, New Hampshire, New York and Idaho. In general, they have more complicated

experience formulas, exclude fewer factors from the charging method, and have complicated their systems with add-ons and surtaxes. The three equally weighted factors considered in this sub-index are experience rating formulas, charging methods, and a host of smaller factors aggregated into one variable.

### **Experience Rating Formula**

A business's experience rating formula determines the rate the firm must pay—whether it will lean towards the minimum rate or maximum rate of the given rate schedule.

There are four basic experience formulas—contribution, benefit, payroll and state experience. The first three experience formulas—the contribution, benefit and payroll—are based solely on the business's experience and are therefore non-neutral by design. However, the final variable—state experience—is a positive mitigating factor because all businesses are treated equally. In other words, the state experience is not tied to the experience of any one business; therefore, it is a more neutral factor. This sub-index penalizes states that depend on the contribution, benefit and payroll experience variables while rewarding states with the state experience variable.

### **Charging Methods and Benefits Excluded From Charging**

A business's experience rating will vary depending on which charging method the state government uses. When a former employee applies for unemployment benefits, the benefits paid to the employee must be charged to a previous employer. There are three basic charging methods:

1. **Charging Most Recent or Principal Employer:** Thirteen states charge all the benefits to one employer, usually the most recent.
2. **Charging Base-Period Employers in Inverse Chronological Order:** Six states charge all base-period employers in inverse chronological order. This means that all employers within a base period of time (usually the last year, sometimes longer) will have the benefits charged against them with the most recent employer being charged the most.
3. **Charging in Proportion to Base-Period Wages:** Thirty-one states charge in proportion to base period wages. This means that all employers within a base-period of time (usually the last year, sometimes longer) will have the benefits charged against them in proportion to the wages they paid.



None of these charging methods could be called neutral, but at the margin, charging the most recent or principal employer is the least neutral because the business faced with the necessity of laying off employees knows it will bear the full benefit charge. The most neutral of the three is the “charging in proportion to base-period wages” since there is a higher probability of sharing the benefit charges with previous employers.

As a result, the 31 states that charge in proportion to base-period wages receive the best score. The 13 states that charge the most recent or principal employer receive the worst score. The six that charge base-period employers in inverse chronological order receive a median score.

Many states also recognize that certain benefit costs should not be charged to employers, especially if the separation is beyond the employer’s control. Therefore, this sub-index also accounts for six types of exclusions from benefit charges.

1. Benefit award reversed
2. Reimbursements on combined wage claims
3. Voluntary leaving
4. Discharge for misconduct
5. Refusal of suitable work
6. Continues to work for employer on part-time basis

States are rewarded for each of these exclusions because they nudge a UI system toward neutrality. For instance, if benefit charges were levied for employees who voluntarily quit, then industries with high turnover rates, such as retail, would be hit disproportionately harder. States that receive the best scores in this category are Ohio, Utah, Vermont, Oregon, Louisiana, Delaware, Missouri and Arizona. Ohio receives a perfect score by charging in proportion to base-period wages and including all six benefit exclusions. On the other hand, the states that receive the worst scores are Alaska, New Hampshire, Kentucky, Nevada, New York, Rhode Island and Virginia. All but Alaska charge the most recent or principal employer and forbid most benefit exclusions.<sup>44</sup>

### Other Significant Issues

Five of the eight variables in this catch-all category of the sub-index deal with taxes levied on top of the UI tax. Not all were triggered during 2008, but states are penalized in this sub-index if they are on the books.

Overall, the states that receive the best scores in this category are Kansas, Michigan, Arizona, Georgia, Missouri, Ohio and Vermont. Louisiana, New Jersey and Rhode Island scored the worst.

#### *Solvency Tax*

These taxes are levied on employers when a state’s unemployment fund falls below some defined level.

Seventeen states have a solvency tax on the books though they fall under different names, such as Solvency Adjustment Tax (Alaska), Supplemental Assessment Tax (Delaware), Emergency Tax (New Hampshire), Subsidiary Tax (New York) and Fund Building Tax (Virginia).

#### *Taxes for Socialized Costs or Negative Balance Employer*

These are levied on employers when the state desires to recover benefit costs above and beyond the UI tax collections based on the normal experience rating process. Ten states have these taxes on the books though they fall under different names: Shared Cost Assessment Tax (Alabama) and Graduated Social Cost Factor Rate Tax (Washington).

#### *Loan and Interest Repayment Surtaxes*

Levied on employers when a loan is taken from the federal government or when bonds are sold to pay for benefit costs, these taxes are of two general types. The first is a tax to pay off the federal loan or bond issue. The second is a tax to pay the interest on the federal loan or bond issue. States are not allowed to pay interest costs directly from the state’s unemployment trust fund. Twenty-one states have these taxes on the books though they fall under several names such as: Advance Interest Tax and Bond Assessment Tax (Colorado), Temporary Emergency Assessment Tax (Delaware) and Unemployment Obligation Assessment (Texas), to name a few.

#### *Reserve Taxes*

Reserve taxes are levied on employers to be deposited in a reserve fund separate from the

### NEW JERSEY

New Jersey, which ranks 50<sup>th</sup> out of 50 states, has a tax code that reads like a “What Not To Do” for legislators. On the Corporate Tax Index, New Jersey earns its 39<sup>th</sup> rank by having the 7<sup>th</sup> highest rate in the country, plus restrictive carry-forward rules. It then tries to paper over its onerous corporate tax system by offering tax credits for jobs, research and investment. On the Sales Tax Index, New Jersey earns its 41<sup>st</sup> ranking with a 7% statewide rate, the highest of any state without local option sales taxes. New Jersey scores third to last on the Individual Income Tax Index, because its income tax code is somewhat less damaging than California’s and Maryland’s. On the Property Tax Index, New Jersey scores dead last, with residents paying more property tax per capita than in any other state. Only New Jersey’s unemployment insurance tax is on par with the national average, ranking 24<sup>th</sup> best.

<sup>44</sup> Alaska is the only state not to use benefit payments in its formula but instead the variation in an employer’s payroll from quarter to quarter. This is an extreme violation of tax neutrality since any decision by the employer or employee that would affect payroll may trigger higher UI tax rates. As a result, Alaska scores the worst of all states in this sub-index.

unemployment trust fund. Since the fund is separate, the interest earned on it is often used to create other funds for purposes such as job training and/or paying the costs of the reserve tax's

collection. Five states have these taxes on the books, including: Nebraska (State UI tax), Idaho (Reserve Tax) and North Carolina (Reserve Fund Tax).

**Table 7**  
**Property Tax Index, 2006 – 2009**

State	FY 2009 State Business Tax Climate Index		FY 2008 State Business Tax Climate Index		Change from 2008 to 2009		FY 2007 State Business Tax Climate Index		FY 2006 State Business Tax Climate Index	
	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank
U.S.	5.00	—	5.00	—	5.00	—	5.00	—	5.00	—
Alabama	5.83	13	5.83	13	0.00	0	5.60	16	6.34	7
Alaska	5.11	27	5.25	21	–0.13	–6	5.54	18	5.48	19
Arizona	6.41	4	6.48	5	–0.08	1	6.21	7	6.25	8
Arkansas	5.45	18	5.68	17	–0.23	–1	5.95	11	6.09	11
California	5.82	15	5.77	15	0.05	0	5.59	17	5.67	16
Colorado	6.28	6	6.23	7	0.05	1	6.06	9	6.13	10
Connecticut	3.05	49	3.04	50	0.01	1	2.81	49	2.12	50
Delaware	6.16	8	6.19	8	–0.03	0	6.31	5	6.48	5
Florida	5.44	19	5.58	19	–0.14	0	4.79	31	4.76	29
Georgia	4.31	36	4.41	35	–0.09	–1	5.22	23	5.26	22
Hawaii	6.14	9	6.54	4	–0.40	–5	6.29	6	6.42	6
Idaho	6.50	3	6.81	2	–0.31	–1	6.83	3	6.90	3
Illinois	4.02	41	3.91	40	0.11	–1	4.19	39	4.13	38
Indiana	6.27	7	5.66	18	0.61	11	4.88	29	4.90	28
Iowa	4.48	33	4.43	34	0.05	1	4.73	33	4.70	31
Kansas	4.54	32	4.32	36	0.22	4	4.63	34	4.60	33
Kentucky	5.43	20	5.38	20	0.05	0	5.70	13	4.65	32
Louisiana	5.20	22	4.75	30	0.46	8	5.08	25	5.22	23
Maine	4.07	40	3.85	41	0.22	1	4.22	38	4.07	39
Maryland	4.38	34	4.11	39	0.27	5	3.84	41	3.87	40
Massachusetts	3.59	44	3.57	44	0.01	0	3.70	43	3.67	43
Michigan	5.16	25	5.15	24	0.01	–1	4.52	35	4.94	26
Minnesota	5.79	17	5.95	11	–0.16	–6	5.65	15	5.70	15
Mississippi	4.89	29	4.95	29	–0.06	0	5.29	21	5.36	21
Missouri	6.02	11	6.01	10	0.01	–1	5.84	12	5.95	13
Montana	6.03	10	6.02	9	0.02	–1	5.18	24	5.12	24
Nebraska	3.38	48	3.31	48	0.08	0	3.52	45	3.45	46
Nevada	5.79	16	5.83	14	–0.04	–2	5.65	14	5.71	14
New Hampshire	4.10	39	4.48	32	–0.38	–7	4.74	32	4.33	37
New Jersey	2.90	50	3.17	49	–0.27	–1	3.34	46	3.16	47
New Mexico	7.16	1	7.13	1	0.03	0	7.50	1	7.69	1
New York	3.57	45	3.76	42	–0.19	–3	3.73	42	3.60	45
North Carolina	4.15	37	4.14	37	0.01	0	3.85	40	3.70	42
North Dakota	6.29	5	6.27	6	0.02	1	6.62	4	6.67	4
Ohio	3.55	46	3.60	43	–0.04	–3	3.16	47	3.12	48
Oklahoma	5.19	23	5.16	23	0.03	0	5.42	20	5.56	18
Oregon	5.83	14	5.72	16	0.10	2	6.03	10	6.07	12
Pennsylvania	3.41	47	3.45	46	–0.03	–1	3.70	44	3.66	44
Rhode Island	3.72	43	3.35	47	0.37	4	2.70	50	2.54	49
South Carolina	5.12	26	5.09	27	0.03	1	4.91	28	4.93	27
South Dakota	5.85	12	5.84	12	0.00	0	6.10	8	6.18	9
Tennessee	4.15	38	4.14	38	0.01	0	4.40	37	4.50	34
Texas	4.71	30	4.61	31	0.10	1	4.49	36	4.43	36
Utah	6.64	2	6.66	3	–0.02	1	7.00	2	7.10	2
Vermont	3.73	42	3.49	45	0.24	3	3.06	48	3.76	41
Virginia	4.99	28	5.19	22	–0.20	–6	4.97	26	4.43	35
Washington	5.24	21	5.12	26	0.12	5	4.91	27	4.96	25
West Virginia	5.19	24	5.13	25	0.06	1	5.46	19	5.56	17
Wisconsin	4.58	31	4.47	33	0.11	2	4.81	30	4.73	30
Wyoming	4.35	35	5.00	28	–0.64	–7	5.28	22	5.37	20
D.C.	4.29	—	4.09	—	0.20	—	4.36	—	4.53	—

**Note:** The higher the score, the more favorable a state's tax system is for business. All scores are for fiscal years.

**Source:** Tax Foundation

### *Surtaxes for UI Administration or Non-UI Purposes*

Thirty states levy surtaxes on employers, usually to fund administration but sometimes for job training or special improvements in technology. They are often deposited in a fund outside of the state's unemployment fund. Some of the names they go by are Job Training Assessment Tax (Arizona), Social Charge Rate Tax (Louisiana), Reemployment Service Fund Tax (New York), Wage Security Tax (Oregon), Investment South Dakota Future Fee Tax (South Dakota) and Job Skills Fee (Tennessee).

---

*Real and personal property taxes are a contentious subject at the state and local levels as individuals and businesses protest rising tax bills caused by revaluations of residential and business property. In fact, the Tax Foundation's Survey of Tax Attitudes found that local property taxes are perceived as the second most unfair state or local tax.*

---

### *Temporary Disability Insurance*

A handful of states—California, New Jersey, Rhode Island, Hawaii and New York—have established a temporary disability insurance (TDI) program that augments the UI program by extending benefits to those unable to work because of sickness or injury. No separate tax funds them; the money comes right out of the state's unemployment fund, and because the balance of the fund triggers various taxes, the TDIs are included as a negative factor in the calculation of this sub-index.

### *Voluntary Contributions*

Twenty-seven states allow businesses to make voluntary contributions to the unemployment trust fund. In most cases, these contributions are rewarded with a lower rate schedule, often saving the business more money in taxes than was paid through the contribution. The Index rewards states that allow voluntary contributions because firms are able to pay when they can best afford to instead of when they are struggling. This

provision helps to mitigate the non-neutralities of the UI tax.

### *Time-Period to Qualify for Experience Rating*

Newly formed businesses, naturally, do not qualify for an experience rating because they simply have not been around long enough. Federal rules stipulate that states can levy a "new employer" rate for one to three years, but no less than one year.

From a neutrality perspective, however, this new employer rate is non-neutral in almost all cases since the rate is higher than the lowest rate schedule. The longer this rate is in effect, the worse the non-neutrality. As such, the Index rewards states with the minimum one year required to earn an experience rating and penalizes states that require the full three years.

## Property Tax Index

The Property Tax Index is the fifth and final component index that comprises the 2009 State Business Tax Climate Index. The Property Tax Index is comprised of taxes levied on the wealth of individuals and businesses. These include taxes on real and personal property, net worth, and the transfer of assets.

Real and personal property taxes are a contentious subject at the state and local levels as individuals and businesses protest rising tax bills caused by revaluations of residential and business property. In fact, the Tax Foundation's Survey of Tax Attitudes found that local property taxes are perceived as the second most unfair state or local tax.<sup>45</sup> Taxes increase as property values rise unless new, higher assessments are matched by a decrease in the rate.

Property taxes are especially important to businesses because the tax rate on commercial property is generally higher than on residential property. Additionally, localities and states often levy taxes on the personal property or equipment owned by a business. Since property taxes can be a large burden to business, they can have a significant effect on location decisions.

Mark, McGuire and Papke (2000) find taxes that vary from one location to another within a region could be more important determinants of

### INDIANA

Indiana fell three spots in this year's ranking, from 11th to 14th. For fiscal year 2009, Indiana raised its sales tax rate from 6% to 7% and simultaneously enacted significant property tax reduction. The state's ranking fell overall because the Index weights the sales tax more heavily than the property tax. However, in addition to lowering current property tax levies, the reform also included caps on future growth of property taxation; if the reforms cause Indiana's property taxes to grow at a slower rate than the national average in future years, that is likely to improve Indiana's score over time.

45 Andrew Chamberlain and Scott A. Hodge, "2007 Annual Survey of U.S. Attitudes on Tax and Wealth," *Tax Foundation Special Report*, No. 154, April 2007.

intraregional location decisions. They find that higher rates of two business taxes—the sales tax and the personal property tax—are associated with lower employment growth. They estimate that a tax hike on personal property of one percentage point reduces annual employment growth by 2.44 percentage points (Mark et al. 2000).

Personal property taxes are levied on assets of individuals and business. They can be on assets ranging from cars to machinery and equipment to office furniture and fixtures, but are separate from real property taxes which are taxes on land and buildings. These findings provide strong evidence that personal property taxes greatly impact business decisions. Furthermore, these findings suggest that states competing for business would be well served to keep statewide property taxes low so as to be more attractive to business investment. Localities competing for business can put themselves at greater competitive advantage by keeping personal property taxes low as well.

---

*Businesses remitted \$554 billion in state and local taxes in fiscal year 2006, of which 37 percent or \$204.8 billion was for property taxes. The property taxes included tax on real, personal and utility property owned by business.*

---

Bartik (1985), finding that property taxes are a significant factor in business location decisions, estimates that a 10 percent increase in business property taxes decreases the number of new plants opening in a state by between 1 and 2 percent. Bartik (1989) backs up his earlier findings by concluding that higher property taxes negatively affect small business starts. He elaborates that the particularly strong negative effect of property taxes occurs because they are paid regardless of profits, and many small businesses are not profitable in their first few years, so high property taxes would be more influential than profit-based taxes on the start-up decision.

Businesses remitted \$554 billion in state and local taxes in fiscal year 2006, of which 37 percent or \$204.8 billion was for property taxes. The property taxes included tax on real, personal and utility property owned by business (Cline et al. 2007). Obviously property taxes are a significant cost to business. Coupled with the academic

findings that property taxes are the most influential tax in terms of impacting location decisions by businesses, the evidence supports the conclusion that property taxes are a significant factor in a state's business tax climate.

Property taxes are not the only factor included in the Property Tax Index. Taxes on capital stock, intangible property, inventory, real estate transfers, estates, inheritance, generation-skipping transfers and gifts are also included.

The states that score the best on the Property Tax Index are New Mexico, Utah, Idaho, Arizona and North Dakota. These states generally have low rates of property tax whether measured per capita or as a percentage of income. Also, they avoid distortionary taxes like estate, inheritance, gift and other wealth taxes. States that score poorly on the index are New Jersey, Connecticut, Nebraska, Pennsylvania and Ohio. These have high property tax rates and they generally levy several wealth-based taxes (see Table 7).

The Property Tax Index is comprised of two equally weighted sub-indexes devoted to measuring the economic damage of the rates and the tax bases. The rate sub-index consists of property tax collection—measured both per capita and as a percentage of personal income—capital stock tax rates and maximum payments. The base portion consists of dummy variables detailing whether each state levies wealth taxes such as inheritance, estate, gift, inventory, intangible property and other similar taxes. The entire Property Tax Index is weighted 15.48 percent of each state's overall State Business Tax Climate score. See Tables 21 and 22 for details of each state's property taxes.

## Sub-Index #1: The Property Tax Rate

The property tax rate sub-index consists of property tax and capital stock tax sub-indexes. Property taxes are measured by collections per capita and as a percentage of personal income. They are weighted equally and receive 80 percent of the weight of the rate sub-index because of their importance to businesses and individuals and their increasing size and visibility to all taxpayers. States that score the best on the rate sub-index are New Mexico, Kentucky, Alabama, Oklahoma and Delaware. These states generally have low property tax collections and effective rates. They also either lack a capital stock tax, or have one with a low rate and maximum payment. Conversely, states that score poorly have high property tax collections per capita and high effective rates, high capital stock



tax rates and high or no maximum payments. These states include Wyoming, New Jersey, New York, Connecticut and New Hampshire.

### Property Tax Collections and Rates

The property tax rate sub-index is weighted 50 percent for each section: property tax collections per capita and property tax collections as a percent of personal income. Both are included to gain a better understanding of how much each state collects in proportion to its population and its income. Tax collections as a percentage of personal income forms an effective rate that gives taxpayers a sense of how much of their income is devoted to property taxes, and the per capita figure lets them know how much in actual dollar terms they pay in property taxes compared to residents of other states.

---

*The states that score the best on the Property Tax Index are New Mexico, Utah, Idaho, Arizona and North Dakota. These states generally have low rates of property tax whether measured per capita or as a percentage of income. Also, they avoid distortionary taxes like estate, inheritance, gift and other wealth taxes. States that score poorly on the index are New Jersey, Connecticut, Nebraska, Pennsylvania and Rhode Island. These have high property tax rates and they generally levy several wealth-based taxes.*

---

While these measures are not ideal—having effective tax rates of personal and real property for both businesses and individuals would be ideal—they are the best measures available due to the significant data constraints posed by property tax collections. Since a high percentage of property taxes are levied on the local level, there are countless jurisdictions. The sheer number of different localities makes data collection almost impossible. The few studies that tackle the subject use representative towns or cities instead of the entire state. Thus, the best source for data on

property taxes is the Census Bureau since it can compile the data and reconcile definitional problems.

States that maintain low effective rates and low collections per capita are more likely to promote growth than states with high rates and collections. States that score the best on this sub-index have low collections per capita and low effective rates. They include Alabama, Oklahoma, New Mexico, Arkansas and Delaware. States that score poorly have high collections per capita and high effective rates and include New Jersey, New Hampshire, Vermont, Wyoming and Connecticut.

### Property Tax Collections Per Capita

Property tax collections per capita are calculated by dividing property taxes collected in each state (obtained from the Census Bureau) by population. The states that pay the most property tax per capita are New Jersey (\$2,642), Connecticut (\$2,393), New Hampshire (\$2,320), Wyoming (\$2,175) and New York (\$2,124). The states that collect the least per capita are Alabama (\$477), Arkansas (\$527), New Mexico (\$539), Oklahoma (\$562) and Kentucky (\$620).

### Effective Property Tax Rate

Property tax collections as a percent of personal income are derived by dividing the Census Bureau's figure for total property tax collections by personal income in each state. This provides an effective property tax rate. States with the highest effective rates and therefore the worst scores are Vermont (5.12 percent), New Hampshire (5.05 percent), New Jersey (4.88 percent), Maine (4.71 percent) and Wyoming (4.55 percent). States that score well with low effective tax rates are Alabama (1.31 percent), Oklahoma (1.50 percent), Delaware (1.53 percent), New Mexico (1.55 percent) and Arkansas (1.63 percent).

### Capital Stock Taxes

Capital stock taxes (commonly called franchise taxes) are levied on the wealth of a corporation, usually defined as net worth. They are often levied in addition to corporate income taxes, adding a duplicate layer of taxation and compliance for many corporations. Corporations that find themselves in financial trouble must use precious cash flow to pay their capital stock tax. In assessing capital stock taxes, the sub-index accounts for three variables: the capital stock tax rate, maximum payment and capital stock tax versus corporate income tax dummy variable. The capital stock tax sub-index is 20 percent of the total rate sub-index.

---

### *Capital Stock Tax Rate*

This variable measures the rate of taxation as levied by the 22 states with a capital stock tax. Legislators have come to realize the damaging effects of capital stock taxes, and many states are reducing or repealing them. West Virginia is phasing its capital stock rate down from 0.7 percent to 0.21 percent, which level will be reached in 2013. Pennsylvania and Kansas are in the process of phasing out theirs entirely. States with the highest capital stock tax rates for 2008 include West Virginia (0.55 percent), Connecticut (0.31 percent), Louisiana and Arkansas (0.3 percent), and Pennsylvania (0.289 percent).

---

*West Virginia is phasing its capital stock rate down from 0.7 percent to 0.21 percent, which level will be reached in 2013. Pennsylvania and Kansas are in the process of phasing out theirs entirely. States with the highest capital stock tax rates for 2008 include West Virginia (0.55 percent), Connecticut (0.31 percent), Louisiana and Arkansas (0.3 percent), and Pennsylvania (0.289 percent).*

---

### *Maximum Capital Stock Tax Payment*

Nine states mitigate the negative economic impact of the capital stock tax by placing a cap on the maximum capital stock tax payment. These states include Alabama, Connecticut, Delaware, Georgia, Illinois, Kansas, North Carolina, Oklahoma and Oregon, and they receive the highest score on this variable.

### *Capital Stock Tax versus Corporate Income Tax*

Some states mitigate the negative economic impact of the capital stock by allowing corporations to pay the higher of the two taxes. These states are Connecticut, New York, Ohio and Rhode Island, and they receive the highest score on this variable. States that do not have a capital stock get the best scores in this sub-index while the remaining nineteen states that force companies to pay both score the lowest.

## Sub-Index #2: The Property Tax Base

The property tax base sub-index is 50 percent of the total Property Tax Index and is composed of dummy variables listing the different types of property taxes each state levies. Seven taxes are included and each is equally weighted. Arizona, Colorado, Idaho, Missouri, Montana, New Mexico, North Dakota, Utah and Wyoming receive perfect scores because they do not levy any of the seven taxes. Maryland, Nebraska, North Carolina, Pennsylvania and Tennessee score worst because they impose many of the taxes.

### Personal Property Taxes

#### *Intangible Property Tax*

This dummy variable punishes those states that impose taxes on intangible personal property. Intangible personal property includes things such as stocks, bonds and other intangibles such as trademarks. This tax can be highly harmful to businesses that hold large amounts of their own or other companies' stock and that have valuable trademarks. Ten states levy this punitive tax: Alabama, Georgia, Iowa, Louisiana, Mississippi, North Carolina, Ohio, Pennsylvania, Tennessee and Texas.

---

*Each year some businesses, especially those that have not spent a sufficient sum on estate tax planning and on large insurance policies, find themselves unable to pay their estate taxes, either federal or state. Usually they are small-to-medium sized family-owned businesses where the death of the owner occasions a surprisingly large tax liability.*

---

#### *Inventory Tax*

Levied on the value of a company's inventory, the inventory tax is especially harmful to large retail stores and other businesses that store large amounts of merchandise. Inventory taxes are highly distortionary because they force companies to make decisions about production that are not entirely based on economic principles, but rather on how to pay the least amount of tax on goods

produced. Inventory taxes also create strong incentives for companies to locate inventory in states where they can avoid these harmful taxes. Fifteen states levy inventory taxes.

### Asset Transfer Taxes

Five taxes levied on the transfer of assets are part of the Property Tax Index base. These taxes all increase the cost and complexity of transferring wealth and hurt a state's business climate. These harmful effects can be particularly acute in the case of small, family-owned businesses. The five taxes are real estate transfer taxes, estate taxes, inheritance taxes, generation-skipping taxes and gift taxes. Thirty-five states and the District of Columbia levy taxes on the transfer of real estate, adding to the cost of purchasing real property and increasing the complexity of real estate transactions. This tax is harmful to businesses that transfer real property often.

---

*The purpose of the Tax Foundation's State Business Tax Climate Index is to aid business leaders and government policymakers in their determination of whether a state's tax system enhances or harms the competitiveness of the state's business environment.*

---

The 2001 federal tax cut, the Economic Growth and Tax Relief Reconciliation Act (EGTRRA), phased out the federal estate tax by 2010, and lowered its rate in the intervening years, although it will be reinstated in 2011 in the same form as it existed in 2001. Before the phase-out, most states levied an estate tax that piggy-backed on the federal system. Since the federal system allowed for a credit for state estate taxes paid, the federal government was essentially paying the states' estate tax collections, and individuals did not object because their tax liability was unchanged. When the federal government changed its system, states began to decouple to save a substantial source of revenue. The 33 states that have allowed the state death tax credit to expire without decoupling from the federal system or enacting their own estate tax get a positive score. The federal credit was completely phased out as of 2005. Seventeen states have decoupled from the federal system to maintain the

revenue stream of estate taxes by either reverting to pre-EGTRRA rules or creating their own stand-alone system. These states are punished for increasing complexity.

---

*While taxes are a fact of life, not all tax systems are created equal. States should strive to create tax systems that have a broad base and a low rate. Ultimately, that means that states must strive for tax systems that are economically neutral—systems that do not favor one economic activity over another—and systems that promote economic growth by avoiding excessive taxes on business activities and keeping the cost of complying with the tax system as low as possible.*

---

Each year some businesses, especially those that have not spent a sufficient sum on estate tax planning and on large insurance policies, find themselves unable to pay their estate taxes, either federal or state. Usually they are small-to-medium sized family-owned businesses where the death of the owner occasions a surprisingly large tax liability.

Inheritance taxes are similar to estate taxes, but they are levied on the heir of an estate, instead of on the estate itself. Therefore, a person could inherit a family-owned company from his or her parents and be forced to downsize it, or sell part or all of it in order to pay the heir's inheritance tax. Eight states have inheritance taxes and are punished because the inheritance tax causes economic distortions.

Another estate-style tax, the generation-skipping tax, is imposed on people when they bequeath assets to grandchildren. Only Nebraska has the tax now that the federal credit has expired. Similarly, three states, Connecticut, North Carolina and Tennessee, have a gift tax and score poorly. (Louisiana's gift tax expired on January 1, 2008, improving its Property Tax Index score for 2008.) Gift taxes are designed to stop individuals' attempts to avoid the estate tax by giving their estates away before they die. Generation-skipping

and gift taxes are negatives to a state's business tax climate because they also heavily impact individuals who have sole proprietorships, S-corps and LLCs.

## Conclusion

The purpose of the Tax Foundation's State Business Tax Climate Index is to aid business leaders and government policymakers in their determination of whether a state's tax system enhances or harms the competitiveness of the state's business environment. The economic literature shows that taxes do matter a great deal, and the Index reduces many complex considerations to an easy-to-use ranking. But businesses must grapple with a wide assortment of other issues, such as proximity to consumers, raw materials or a skilled labor pool. These concerns may seem more important than a good tax system, but taxes can positively or negatively affect a business's position with regard to these very resources.

---

*States that score poorly can use the Index to pinpoint the improvements that would enhance their competitiveness the most.*

---

While taxes are a fact of life, not all tax systems are created equal. States should strive to create tax systems that have a broad base and a low rate. Ultimately, that means that states must strive for tax systems that are economically neutral—systems that do not favor one economic activity over another—and systems that promote economic growth by avoiding excessive taxes on business activities and keeping the cost of complying with the tax system as low as possible.

The 2009 State Business Tax Climate Index highlights those factors that make states' tax climates more or less competitive than other

states' tax climates. States that score poorly can use the Index to pinpoint the improvements that would enhance their competitiveness the most. States that score well can also use the Index to determine where they gain a competitive advantage and work to strengthen their advantage in those areas, or work to improve the factors on which they do not score as well.

---

*In a highly competitive global market, states need to make their tax systems friendly to business in order to facilitate the expansion and growth of business. A simple tax system that is fair to all businesses is the best way for states to have a competitive business tax climate.*

---

In a highly competitive global market, states need to make their tax systems friendly to business in order to facilitate the expansion and growth of business. A simple tax system that is fair to all businesses is the best way for states to have a competitive business tax climate.

## Changes to Methodology

The 2009 SBTCl eliminated one variable included in previous indices (deductibility of foreign income taxes paid from the individual income tax) because of lack of differentiation among states. Additionally, marriage penalty scoring was altered to give credit for allowing married couples to file separately on a single return only if a state imposes a marriage penalty. These changes were backcast into the previous year results included in this report, resulting in modest changes to states' past year ranks. Past years' scores and ranks also changed slightly due to updated data.



## Appendix 1: Pending Tax Changes Not Reflected in the 2009 State Business Tax Climate Index

The 2009 State Business Tax Climate Index depicts each state's tax system as it stood on July 1, 2008 — the first day of the 2009 fiscal year. We note here the changes that have been enacted into law but were not yet effective on July 1, and so are not reflected in the Index. No definite claims can be made about how a particular state change could affect a future ranking because other states may improve or damage their business tax climates in the meantime; however, we categorize changes here as ones that are likely to improve or worsen a state's tax climate.

### Changes Likely to Improve a State's Tax Climate

**Kansas:** Kansas continues to phase out its franchise tax, which is categorized with the capital stock taxes in the Property Tax Index. The franchise tax rate, set at 0.125 percent for 2007 and before, is 0.09375 percent for 2008 and will continue to fall through 2010. In 2011 the tax will be fully repealed. Kansas will likely see improvement in its score on the Property Tax Index as the tax is phased out. When the tax is completely abolished, Kansas will join the other 28 states that do without a capital stock-style tax.

**Massachusetts:** Effective on January 1, 2009, Massachusetts will adopt combined reporting for its corporate income tax, and a "check the box" rule that prohibits firms from electing one corporate status for federal tax purposes and another for Massachusetts tax purposes. Additionally, the state will begin phasing down its corporate income tax rate in 2010, eventually reducing the rate to 8 percent (in 2012 and beyond) from 9.5 percent today. There are good arguments for and against the soundness of combined reporting, which is not rated in the SBTCl; as such, Massachusetts' corporate income tax index score can be expected to improve once the tax rate starts falling in 2010.

**Oklahoma:** Oklahoma's top income tax rate is in the middle of a five year phase-down. In 2006 the top rate stood at 6.25 percent on income over \$8,700. Currently, the top rate is 5.5 percent and will continue to fall until it reaches 5.25 percent in 2009—a full percentage point lower than in 2006. Oklahoma's score on the Individual Income Tax Index and its overall score will likely improve as the rate cut continues, unless other states take an equally aggressive rate-cutting path.

**Pennsylvania:** Pennsylvania began the phase-out of its franchise tax in 2000 when it was one of the highest in the nation, at 1.1 percent. For 2008 the rate rests at 0.289 percent. The tax will be fully abolished in 2011. Pennsylvania's Property Tax Index score and its overall score should improve as the tax is phased out. Pennsylvania will join the 28 states and Kansas in 2011 as states that have no capital stock tax.

**Rhode Island:** As noted within this report, Rhode Island is phasing in an optional flat-rate income tax. This year's optional rate is at 7.0%, and the rate will fall by 0.5% per year until it reaches 5.5% in 2011. As the rate drops, the optional flat tax will become attractive to more and more Rhode Island filers, improving the state's tax climate.

**West Virginia:** The state continues to phase down its corporate income and franchise taxes. In 2006 and prior, West Virginia had one of the country's highest corporate income tax rates, at 9%. The rate is now 8.75% and will fall to 8.5% in 2009, 7.75% in 2012, 7% in 2013, and 6.5% in 2014. Its franchise tax is still the highest in the country at 0.55% (formerly 0.7%), but it will fall gradually until it reaches 0.21% in 2013. As these rates continue to fall, West Virginia should see continued improvement on its Corporate Income and Property Tax Index scores.

#### LOUISIANA

Unlike most states with significant energy resources, Louisiana has all major taxes and rates in the bottom half of tax climates. Its sales tax, ranking 46<sup>th</sup> nationally, is especially bad; including local option rates, it averages over 8%, and it covers many business inputs. On the bright side, the state has repealed its gift tax, effective July 1, 2008. With this repeal, Louisiana moved from 30<sup>th</sup> to 22<sup>nd</sup> on the property tax index. Overall, Louisiana moved up two spots, from 35<sup>th</sup> to 33<sup>rd</sup>.

### Changes Likely to Hurt a State's Tax Climate

**District of Columbia:** In March 2008, the District of Columbia council voted to raise the cigarette tax by \$1 per pack, to \$2. The increase took effect on October 1, meaning that the District's tax on cigarettes is now nearly seven times higher than Virginia's but equal to Maryland's. Cigarette taxes are counted in the Sales Tax Index, and so it is likely that this increase will hurt the District's rating for next year.

**Hawaii:** Hawaii also has a pending cigarette tax increase. Its cigarette tax on July 1, 2007 was \$1.60 per pack. This year's rate is \$1.80, and the rate will rise by twenty cents each year until it reaches \$2.60 in 2011. Unless other states raise

---

their rates even faster, Hawaii's Sales Tax ranking is also likely to fall.

### Changes With an Uncertain Effect On a State's Tax Climate

**Indiana:** Indiana adopted a major tax reform that is effective for FY 2009, with several components. The reform raised the state sales tax from 6% to 7%, imposed significant reductions in property tax rates, and capped future property tax levies at a fixed percentage of value. As a result of this reform, Indiana's ranking fell from 11<sup>th</sup> to 14<sup>th</sup> for 2009, principally because the Index weights sales taxes more heavily than property taxes. However, if the property tax cap holds Indiana's property tax increases below the national average in future years, its ranking may improve over time.

**Ohio:** Ohio continues the phase in and phase out of several taxes. In the coming year, the Corporate

Activities Tax (CAT) will continue to be phased in as its rate increases, but the state's corporate income tax will be lowered as well. The effect of these two countervailing forces is uncertain, and much like Michigan, depends largely on the actions of other states. The full effect on Ohio's ranking, both on the Corporate Tax Index and overall, will not be completely known until 2010, when the phase in of the CAT is complete and the corporate income tax is fully phased out. Ohio's score on the Individual Income Tax Index, however, should improve as the state's income tax rates continue to fall through 2010. The top rate, which began at 7.25 percent in 2004 on income over \$200,000, will fall below 6.0 percent by 2010. However, extensive local income taxes in Ohio mute much of the potential benefit from the state rate cuts.

## Appendix 2: Components of the State Business Tax Climate Index

*Table 8*  
*State Corporate Tax Rates*  
*As of July 1, 2008*

State	Corporate Income Tax Rates and Brackets			Gross Receipts Tax Rate (a)
Alabama	6.5%	>	\$0	
Alaska	1%	>	\$0	
	2%	>	\$10,000	
	3%	>	\$20,000	
	4%	>	\$30,000	
	5%	>	\$40,000	
	6%	>	\$50,000	
	7%	>	\$60,000	
	8%	>	\$70,000	
	9%	>	\$80,000	
	9.4%	>	\$90,000	
Arizona	6.968%	>	\$0	
Arkansas	1%	>	\$0	
	2%	>	\$3,000	
	3%	>	\$6,000	
	5%	>	\$11,000	
	6%	>	\$25,000	
	6.5%	>	\$100,000	
California	8.84%	>	\$0	
Colorado	4.63%	>	\$0	
Connecticut	7.5%	>	\$0	
Delaware	8.7%	>	\$0	0.576%
Florida	5.5%	>	\$0	
Georgia	6%	>	\$0	
Hawaii	4.4%	>	\$0	
	5.4%	>	\$25,000	
	6.4%	>	\$100,000	
Idaho	7.6%	>	\$0	
Illinois	7.3%	>	\$0	
Indiana	8.5%	>	\$0	
Iowa	6%	>	\$0	
	8%	>	\$25,000	
	10%	>	\$100,000	
	12%	>	\$250,000	
Kansas	4%	>	\$0	
	7.35%	>	\$50,000	
Kentucky	4%	>	\$0	0.095%
	5%	>	\$50,000	
	6%	>	\$100,000	
Louisiana	4%	>	\$0	
	5%	>	\$25,000	
	6%	>	\$50,000	
	7%	>	\$100,000	
	8%	>	\$200,000	
Maine	3.5%	>	\$0	
	7.93%	>	\$25,000	
	8.33%	>	\$75,000	
	8.93%	>	\$250,000	
Maryland	8.25%	>	\$0	
Massachusetts (b)	9.5%	>	\$0	
Michigan (c)	6.04%	>	\$0	0.98%
Minnesota	9.8%	>	\$0	

Mississippi	3%	>	\$0	
	4%	>	\$5,000	
	5%	>	\$10,000	
Missouri	6.25%	>	\$0	
Montana	6.75%	>	\$0	
Nebraska	5.58%	>	\$0	
	7.81%	>	\$50,000	
Nevada		None		
New Hampshire (d)	8.5%	>	\$50,000	0.75%
New Jersey(e)	6.76%	>	\$0	
	7.8%	>	\$50,000	
	9.36%	>	\$100,000	
New Mexico	4.8%	>	\$0	
	6.4%	>	\$500,000	
	7.6%	>	\$1,000,000	
New York	7.1%	>	\$0	
North Carolina	6.9%	>	\$0	
North Dakota	2.6%	>	\$0	
	4.1%	>	\$3,000	
	5.6%	>	\$8,000	
	6.4%	>	\$20,000	
	6.5%	>	\$30,000	
Ohio	2.04%	>	\$0	0.208%
	3.4%	>	\$50,000	
Oklahoma	6%	>	\$0	
Oregon	6.6%	>	\$0	
Pennsylvania	9.99%	>	\$0	
Rhode Island	9%	>	\$0	
South Carolina	5%	>	\$0	
South Dakota		None		
Tennessee	6.5%	>	\$0	
Texas		None		1.0%
Utah	5%	>	\$0	
Vermont	6%	>	\$0	
	7%	>	\$10,000	
	8.75%	>	\$25,000	
Virginia	6%	>	\$0	
Washington		None		0.484%
West Virginia	8.75%	>	\$0	
Wisconsin	7.9%	>	\$0	
Wyoming		None		
District of Columbia	9.98%	>	\$0	

Note: Corporations pay many types of taxes, of which the corporate income tax is usually the most important for the business tax climate. However, some states levy other important business taxes such as the franchise tax and capital stock tax. Many of these are “wealth taxes” with a tax base consisting of capital assets, stocks, property, etc. The State Business Tax Climate Index tallies these in the Property Tax Index rather than in the Corporate Tax Index.

(a) Most states collect tax as a percentage of gross receipts from public utilities and some other sectors, and most states have a business license fee or other fixed dollar amount that all businesses must pay, and sometimes those are called gross receipts taxes. Shown here are only the states that tax all business broadly as a percentage of gross receipts.

(b) Includes 14 percent surtax.

(c) Includes 21.99 percent surtax.

(d) New Hampshire has a dual corporate income tax with differing tax bases—the business profit tax (BPT) and business enterprise tax (BET). The BPT has a rate of 8.5 percent if gross income is over \$50,000 and the BET has a rate of 0.75 percent if gross income is over \$150,000 or base (total compensation, interest and dividends paid) over \$75,000.

(e) Includes 4 percent surtax.

Sources: Tax Foundation, Commerce Clearing House, state tax forms.



**Table 9**  
**Business Tax Base Criteria: Credits and Deductions**  
**As of July 1, 2008**

State	Job Credits	Research and Development Credits	Investment Credits	Compensation Expenses Deductible	Cost of Goods Sold Deductible
Alabama	Yes	No	Yes	Yes	Yes
Alaska	No	No	No	Yes	Yes
Arizona	No	Yes	Yes	Yes	Yes
Arkansas	Yes	Yes	Yes	Yes	Yes
California	Yes	Yes	No	Yes	Yes
Colorado	Yes	Yes	Yes	Yes	Yes
Connecticut	Yes	Yes	Yes	Yes	Yes
Delaware	Yes	Yes	Yes	No	No
Florida	Yes	No	Yes	Yes	Yes
Georgia	Yes	Yes	Yes	Yes	Yes
Hawaii	No	Yes	Yes	Yes	Yes
Idaho	Yes	Yes	Yes	Yes	Yes
Illinois	Yes	Yes	Yes	Yes	Yes
Indiana	Yes	Yes	Yes	Yes	Yes
Iowa	Yes	Yes	Yes	Yes	Yes
Kansas	Yes	Yes	Yes	Yes	Yes
Kentucky	Yes	Yes	Yes	No	Yes
Louisiana	Yes	Yes	Yes	Yes	Yes
Maine	Yes	Yes	Yes	Yes	Yes
Maryland	Yes	Yes	Yes	Yes	Yes
Massachusetts	Yes	Yes	Yes	Yes	Yes
Michigan	Yes	No	Yes	Partial	Yes
Minnesota	Yes	Yes	No	Yes	Yes
Mississippi	Yes	No	Yes	Yes	Yes
Missouri	Yes	No	No	Yes	Yes
Montana	Yes	Yes	Yes	Yes	Yes
Nebraska	Yes	Yes	Yes	Yes	Yes
Nevada	n.a.	n.a.	n.a.	n.a.	n.a.
New Hampshire	Yes	No	Yes	No	Yes
New Jersey	Yes	Yes	Yes	Yes	Yes
New Mexico	Yes	Yes	Yes	Yes	Yes
New York	Yes	Yes	Yes	Yes	Yes
North Carolina	Yes	Yes	Yes	Yes	Yes
North Dakota	Yes	Yes	Yes	Yes	Yes
Ohio	Yes	Yes	Yes	No	No
Oklahoma	Yes	No	Yes	Yes	Yes
Oregon	No	Yes	No	Yes	Yes
Pennsylvania	Yes	Yes	No	Yes	Yes
Rhode Island	Yes	Yes	Yes	Yes	Yes
South Carolina	Yes	Yes	No	Yes	Yes
South Dakota	n.a.	n.a.	n.a.	n.a.	n.a.
Tennessee	Yes	No	No	Yes	Yes
Texas	No	Yes	No	Partial (a)	Partial (a)
Utah	Yes	Yes	No	Yes	Yes
Vermont	Yes	Yes	Yes	Yes	Yes
Virginia	Yes	No	No	Yes	Yes
Washington	Yes	Yes	Yes	No	No
West Virginia	Yes	Yes	Yes	Yes	Yes
Wisconsin	No	Yes	Yes	Yes	Yes
Wyoming	n.a.	n.a.	n.a.	n.a.	n.a.
Dist. of Columbia	Yes	No	No	Yes	Yes

(a) Businesses may deduct either compensation or cost of goods sold but not both.  
Source: Tax Foundation, CCH.

**Table 10**  
**Other Business Tax Base Criteria**  
**As of July 1, 2008**

State	Carry-back (Years)	Carry-forward (Years)	Carry-back Cap	Carry-forward Cap
Alabama	0	15	\$0	Unlimited
Alaska	2	20	Unlimited	Unlimited
Arizona	0	5	\$0	Unlimited
Arkansas	0	5	\$0	Unlimited
California	0	10	\$0	Unlimited
Colorado	0	20	\$0	Unlimited
Connecticut	0	20	\$0	Unlimited
Delaware	2	20	\$30,000	Unlimited
Florida	0	20	\$0	Unlimited
Georgia	2	20	Unlimited	Unlimited
Hawaii	2	20	Unlimited	Unlimited
Idaho	2	20	\$100,000	Unlimited
Illinois	0	12	\$0	Unlimited
Indiana	2	20	Unlimited	Unlimited
Iowa	2	20	Unlimited	Unlimited
Kansas	0	10	\$0	Unlimited
Kentucky	0	20	\$0	Unlimited
Louisiana	3	15	Unlimited	Unlimited
Maine	0	20	\$0	Unlimited
Maryland	2	20	Unlimited	Unlimited
Massachusetts	0	5	\$0	Unlimited
Michigan	0	10	\$0	Unlimited
Minnesota	0	15	\$0	Unlimited
Mississippi	2	20	Unlimited	Unlimited
Missouri	2	20	Unlimited	Unlimited
Montana	3	7	Unlimited	Unlimited
Nebraska	0	5	\$0	Unlimited
Nevada	n.a.	n.a.	n.a.	n.a.
New Hampshire	0	10	\$0	\$1,000,000
New Jersey	0	7	\$0	Unlimited
New Mexico	0	5	\$0	Unlimited
New York	2	20	\$10,000	Unlimited
North Carolina	0	15	\$0	Unlimited
North Dakota	0	20	\$0	Unlimited
Ohio	0	20	\$0	Unlimited
Oklahoma	2	20	Unlimited	Unlimited
Oregon	0	15	\$0	Unlimited
Pennsylvania	0	20	\$0	\$3,000,000
Rhode Island	0	5	\$0	Unlimited
South Carolina	0	20	\$0	Unlimited
South Dakota	n.a.	n.a.	n.a.	n.a.
Tennessee	0	15	\$0	Unlimited
Texas	0	5	\$0	Unlimited
Utah	3	15	\$1,000,000	Unlimited
Vermont	0	10	\$0	Unlimited
Virginia	2	20	Unlimited	Unlimited
Washington	3	20	Unlimited	Unlimited
West Virginia	2	20	\$300,000	Unlimited
Wisconsin	0	15	\$0	Unlimited
Wyoming	n.a.	n.a.	n.a.	n.a.
District of Columbia	0	20	\$0	Unlimited

Source: CCH.

*Table 11*  
*Other Business Tax Base Criteria*  
*As of July 1, 2008*

State	Federal Income Used as State Tax Base	Allows Federal ACRS or MACRS Depreciation	Allows Federal Depletion	Throwback Rule	Foreign Tax Deductibility	Corporate AMT	Brackets Indexed for Inflation
Alabama	Yes	Yes	No	Yes	Yes	No	Yes
Alaska	Yes	Yes	Partial	Yes	No	Yes	No
Arizona	Yes	Yes	Yes	No	No	No	Yes
Arkansas	No	Yes	Yes	Yes	Yes	No	No
California	Yes	No	Yes	Yes	No	Yes	Yes
Colorado	Yes	Yes	Yes	Yes	No	No	Yes
Connecticut	Yes	Yes	Yes	No	Yes	No	Yes
Delaware	Yes	Yes	Partial	No	Yes	No	Yes
Florida	Yes	Yes	Yes	No	Yes	Yes	Yes
Georgia	Yes	Yes	Yes	No	No	No	Yes
Hawaii	Yes	Yes	Yes	Yes	Yes	No	No
Idaho	Yes	Yes	Yes	Yes	Yes	No	Yes
Illinois	Yes	Yes	Yes	Yes	Yes	No	Yes
Indiana	Yes	Yes	Yes	Yes	No	No	Yes
Iowa	Yes	Yes	Partial	No	Yes	Yes	No
Kansas	Yes	Yes	Yes	Yes	No	No	No
Kentucky	Yes	Yes	Yes	No	No	No	No
Louisiana	Yes	Yes	Partial	No	Yes	No	No
Maine	Yes	Yes	Yes	Yes	Yes	Yes	No
Maryland	Yes	Yes	Yes	No	Yes	No	Yes
Massachusetts	Yes	Yes	Yes	Yes	No	No	Yes
Michigan	Yes	No	Yes	No	No	No	Yes
Minnesota	Yes	Yes	No	No	No	Yes	Yes
Mississippi	No	Yes	Yes	Yes	No	No	No
Missouri	Yes	Yes	Yes	Yes	Yes	No	Yes
Montana	Yes	Yes	Yes	Yes	No	No	Yes
Nebraska	Yes	Yes	Yes	No	Yes	No	No
Nevada	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
New Hampshire	Yes	Yes	Partial	Yes	No	No	No
New Jersey	Yes	Yes	Yes	No	No	No	No
New Mexico	Yes	Yes	Yes	Yes	Yes	No	No
New York	Yes	Yes	Yes	No	No	Yes	Yes
North Carolina	Yes	Yes	Partial	No	No	No	Yes
North Dakota	Yes	Yes	Yes	Yes	No	No	No
Ohio	Yes	Yes	Yes	No	Yes	No	No
Oklahoma	Yes	Yes	Yes	Yes	No	No	Yes
Oregon	Yes	Yes	No	Yes	No	No	Yes
Pennsylvania	Yes	Yes	Yes	No	No	No	Yes
Rhode Island	Yes	Yes	Yes	Yes	Yes	No	Yes
South Carolina	Yes	Yes	Yes	No	No	No	Yes
South Dakota	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Tennessee	Yes	Yes	Yes	No	Yes	No	Yes
Texas	Yes	Yes	Partial	Yes	Yes	No	Yes
Utah	Yes	Yes	Yes	Yes	No	No	Yes
Vermont	Yes	Yes	Yes	Yes	Yes	No	No
Virginia	Yes	Yes	Yes	No	No	No	Yes
Washington	No	No	No	No	No	No	Yes
West Virginia	Yes	Yes	Yes	No	No	No	Yes
Wisconsin	Yes	Yes	No	Yes	Yes	No	Yes
Wyoming	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
District of Columbia	No	Yes	Yes	Yes	No	No	Yes

Source: CCH.

*Table 12*  
*Individual Income Tax Rates*  
*As of July 1, 2008*

State	Federal Deductibility	Tax Rates and Brackets for Single Filers (a)	Standard Deduction		Personal Exemption (b)		Local Option Income Tax Rate (v)
			Single	Joint	Single	Dependents	
Alabama	Yes	2% > \$0 4% > \$500 5% > \$3,000	\$2,000	\$4,000	\$1,500	\$300	0.19%
Alaska	No	None	n.a.	n.a.	n.a.	n.a.	None
Arizona	No	2.59% > \$0 2.88% > \$10,000 3.36% > \$25,000 4.24% > \$50,000 4.54% > \$150,000	\$4,502	\$9,004	\$2,100	\$2,100	None
Arkansas (k)(r)	No	1% > \$0 2.5% > \$3,700 3.5% > \$7,400 4.5% > \$11,100 6% > \$18,600 7% > \$31,000	\$2,000	\$4,000	\$22 (c)	\$22 (c)	0.06%
California (r)	No	1% > \$0 2% > \$6,827 4% > \$16,815 6% > \$25,544 8% > \$35,460 9.3% > \$44,814 10.3% > \$1,000,000	\$3,516	\$7,032	\$94 (c)	\$294 (c)	None
Colorado	No	4.63% of federal taxable income	n.a.	n.a.	n.a.	n.a.	None
Connecticut	No	3% > \$0 5% > \$10,000	n.a.	n.a.	\$13,000 (e)	\$0	None
Delaware	No	2.2% > \$2,000 3.9% > \$5,000 4.8% > \$10,000 5.2% > \$20,000 5.55% > \$25,000 5.95% > \$60,000	\$3,250	\$6,500	\$110 (c)	\$110 (c)	0.16%
Florida	No	None	n.a.	n.a.	n.a.	n.a.	None
Georgia	No	1% > \$0 2% > \$750 3% > \$2,250 4% > \$3,750 5% > \$5,250 6% > \$7,000	\$2,300	\$3,000	\$2,700	\$3,000	None
Hawaii	No	1.4% > \$0 3.2% > \$2,400 5.5% > \$4,800 6.4% > \$9,600 6.8% > \$14,400 7.2% > \$19,200 7.6% > \$24,000 7.9% > \$36,000 8.25% > \$48,000	\$2,000	\$4,000	\$1,040	\$1,040	None
Idaho (r)	No	1.6% > \$0 3.6% > \$1,237 4.1% > \$2,474 5.1% > \$3,710 6.1% > \$4,987 7.1% > \$6,184 7.4% > \$9,276 7.8% > \$24,736	\$5,450 (s)	\$10,900 (s)	\$3,500 (s)	\$3,500 (s)	None
Illinois	No	3% of federal adjusted gross income with modification.	n.a.	n.a.	\$2,000	\$2,000	None
Indiana	No	3.4% of federal adjusted gross income with modification.	n.a.	n.a.	\$1,000	\$1,000 (i)	1.16%

*Table 12 (continued)*  
*Individual Income Tax Rates*  
*As of July 1, 2008*

State	Federal Deductibility	Tax Rates and Brackets for Single Filers (a)	Standard Deduction		Personal Exemption (b)		Local Option Income Tax Rate (v)
			Single	Joint	Single	Dependents	
Iowa (r)	Yes	0.36% > \$0 0.72% > \$1,379 2.43% > \$2,758 4.5% > \$5,515 6.12% > \$12,411 6.48% > \$20,685 6.8% > \$27,580 7.92% > \$41,370 8.98% > \$62,055	\$1,750	\$4,310	\$40 (c)	\$40 (c)	0.3%
Kansas	No	3.5% > \$0 6.25% > \$15,000 6.45% > \$30,000	\$5,450	\$10,900	\$2,250	\$2,250	None
Kentucky	No	2% > \$0 3% > \$3,000 4% > \$4,000 5% > \$5,000 5.8% > \$8,000 6% > \$75,000	\$2,050 (r)	\$2,050 (r)	\$20 (c)	\$20 (c)	0.76%
Louisiana	Yes	2% > \$0 4% > \$12,500 6% > \$25,000	n.a.	n.a.	\$4,500 (l)	\$1,000	None
Maine (r)	No	2% > \$0 4.5% > \$4,850 7% > \$9,700 8.5% > \$19,450	\$5,450	\$9,100	\$2,850	\$2,850	None
Maryland	No	2% > \$0 3% > \$1,000 4% > \$2,000 4.75% > \$3,000 5% > \$150,000 5.25% > \$300,000 5.5% > \$500,000 6.25% > \$1,000,000	\$2,000 (m)	\$4,000 (m)	\$3,200	\$3,200	2.98%
Massachusetts	No	5.3% and 12% (f)	n.a.	n.a.	\$4,125	\$1,000	None
Michigan	No	4.35% of federal adjusted gross income with modification	n.a.	n.a.	\$3,400 (s)	\$3,400 (s)	0.44%
Minnesota	No	5.35% > \$0 7.05% > \$21,310 7.85% > \$69,990	\$5,450 (s)	\$10,900 (s)	\$3,500 (s)	\$3,500 (s)	None
Mississippi	No	3% > \$0 4% > \$5,000 5% > \$10,000	\$2,300	\$4,600	\$6,000	\$1,500	None
Missouri	Limited	1.5% > \$0 2% > \$1,000 2.5% > \$2,000 3% > \$3,000 3.5% > \$4,000 4% > \$5,000 4.5% > \$6,000 5% > \$7,000 5.5% > \$8,000 6% > \$9,000	\$5,450 (s)	\$10,900 (s)	\$2,100	\$1,200	0.12%
Montana (r)	Limited	1% > \$0 2% > \$2,500 3% > \$4,400 4% > \$6,600 5% > \$9,000 6% > \$11,600 6.9% > \$14,900	\$3,810	\$7,620	\$2,040	\$2,040	None



*Table 12 (continued)*  
**Individual Income Tax Rates**  
*As of July 1, 2008*

State	Federal Deductibility	Tax Rates and Brackets for Single Filers (a)	Standard Deduction		Personal Exemption (b)		Local Option Income Tax Rate (v)
			Single	Joint	Single	Dependents	
Nebraska	No	2.56% > \$0 3.57% > \$2,400 5.12% > \$17,500 6.84% > \$27,000	\$5,450 (r)	\$10,900 (r)	\$106 (c)(n)	\$106 (c)(n)	None
Nevada	No	None	n.a.	n.a.	n.a.	n.a.	None
New Hampshire	No	5% > \$0 (h)	\$2,400	\$4,800	n.a.	n.a.	None
New Jersey	No	1.4% > \$0 1.75% > \$20,000 3.5% > \$35,000 5.525% > \$40,000 6.37% > \$75,000 8.97% > \$500,000	n.a.	n.a.	\$1,000	\$1,500	0.09%
New Mexico	No	1.7% > \$0 3.2% > \$5,500 4.7% > \$11,000 4.9% > \$16,000	\$5,450 (s)	\$10,900 (s)	\$3,500 (s)	\$3,500 (s)	None
New York	No	4% > \$0 4.5% > \$8,000 5.25% > \$11,000 5.9% > \$13,000 6.85% > \$20,000	\$7,500	\$15,000	n.a.	\$1,000	1.7%
North Carolina	No	6% > \$0 7% > \$12,750 7.75% > \$60,000	\$3,000	\$6,000	\$3,500	\$3,500	None
North Dakota (r)	No	2.1% > \$0 3.92% > \$31,850 4.34% > \$77,100 5.04% > \$160,850 5.54% > \$349,700	\$5,450 (s)	\$10,900 (s)	\$3,500 (s)	\$3,500 (s)	None
Ohio	No	0.618% > \$0 1.24% > \$5,000 2.47% > \$10,000 3.09% > \$15,000 3.71% > \$20,000 4.33% > \$40,000 4.94% > \$80,000 5.74% > \$100,000 6.24% > \$200,000	n.a.	n.a.	\$1,450 (r) + \$20 (c)	\$1,450 (r) + \$20 (c)	1.82%
Oklahoma	No	0.5% > \$0 1% > \$1,000 2% > \$2,500 3% > \$3,750 4% > \$4,900 5% > \$7,200 5.5% > \$8,700	\$3,250	\$6,500	\$1,000	\$1,000	None
Oregon (r)	Limited	5% > \$0 7% > \$2,850 9% > \$7,150	\$1,825	\$3,650	\$165 (c)(r)	\$1659 (c)(r)	0.36%
Pennsylvania	No	3.07% > \$0	n.a.	n.a.	n.a.	n.a.	1.25%
Rhode Island (r)	No	3.75% > \$0 7% > \$31,850 7.75% > \$77,100 9% > \$160,850 9.9% > \$349,700	\$5,450	\$8,900	\$3,500	\$3,500	None

*Table 12 (continued)*  
**Individual Income Tax Rates**  
*As of July 1, 2008*

State	Federal Deductibility	Tax Rates and Brackets for Single Filers (a)	Standard Deduction		Personal Exemption (b)		Local Option Income Tax Rate (v)
			Single	Joint	Single	Dependents	
South Carolina (r)	No	2.5% > \$0 3% > \$2,570 4% > \$5,140 5% > \$7,710 6% > \$10,280 7% > \$12,850	\$5,450 (s)	\$10,900 (s)	\$3,500 (s)	\$3,500 (s)	None
South Dakota	No	None	n.a.	n.a.	n.a.	n.a.	None
Tennessee	No	6% > \$0 (h)	n.a.	n.a.	\$1,250	n.a.	None
Texas	No	None	n.a.	n.a.	n.a.	n.a.	None
Utah	No	5.0% > \$0	\$5,450 (s)	\$10,900 (s)	\$2,625 (q)	\$2,625 (q)	None
Vermont (r)	No	3.6% > \$0 7.2% > \$31,850 8.5% > \$77,100 9% > \$160,850 9.5% > \$349,700	\$5,450 (s)	\$10,900 (s)	\$3,500 (s)	\$3,500 (s)	None
Virginia	No	2% > \$0 3% > \$3,000 5% > \$5,000 5.75% > \$17,000	\$3,000	\$6,000	\$930	\$930	None
Washington	No	None	n.a.	n.a.	n.a.	n.a.	None
West Virginia	No	3% > \$0 4% > \$10,000 4.5% > \$25,000 6% > \$40,000 6.5% > \$60,000	n.a.	n.a.	\$2,000	\$2,000	None
Wisconsin (r)	No	4.60% > \$0 6.15% > \$9,510 6.50% > \$19,020 6.75% > \$142,650	\$8,790 (j)	\$15,830 (j)	\$700	\$700	None
Wyoming	No	None	n.a.	n.a.	n.a.	n.a.	None
District of Columbia	No	4.5% > \$0 7% > \$10,000 8.5% > \$40,000	\$4,000	\$4,000	\$1,670	\$1,670	n.a.

(a) Applies to single taxpayers and married people filing separately. Most states double brackets for married filing joint.

(b) Married-joint filers generally receive double the single exemption.

(c) Tax credit.

(e) Maximum equals \$13,000. Value decreases as income increases.

(f) The 12% rate applies to short-term capital gains, long- and short-term capital gains on collectibles and pre-1996 installment sales classified as capital gain income for Massachusetts purposes.

(h) Applies to interest and dividend income only.

(i) Additional \$1,500 dependent child exemption.

(j) Deduction phases out to zero for single filers at \$80,000 and joint filers at \$90,895.

(k) Rates apply to regular tax table. A special tax table is available for low-income taxpayers that reduce their tax payments.

(l) Standard deduction and personal exemptions are combined: \$4,500 for single and married filing separately; \$9,000 married filing jointly and head of household.

(m) The standard deduction is 15 percent of income with a minimum of \$1,500 and a cap of \$2,000 for single filers, married filing separately filers and dependent filers earning more than \$13,333. The standard deduction is capped at \$4,000 for married filing jointly filers, head of household filers and qualifying widowers earning more than \$26,667.

(n) The \$106 personal exemption credit is phased out for filers with adjusted gross income of \$73,000 or more.

(q) Three-fourths federal exemption.

(r) Indexes for inflation.

(s) Deductions and exemptions tied to federal tax system. Federal deductions and exemptions are indexed for inflation.

(v) Weighted average of rates in counties and large municipalities.

**Sources:** Tax Foundation, state tax forms and instructions and Commerce Clearing House.

*Table 13*  
*Individual Income Tax Base Criteria*  
*As of July 1, 2008*

State	Marriage Penalty	Allow Filing Separately on a Single Return	Double Taxation			Indexation		
			Interest	Dividends	Capital Gains	Brackets	Standard Deduction	Exemption
Alabama	No	No	Yes	Yes	Yes	No	No	No
Alaska	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Arizona	No	No	Yes	Yes	Yes	No	Yes	No
Arkansas	Yes	Yes	Yes	Yes	Yes	Yes	No	Yes
California	Yes	No	Yes	Yes	Yes	Yes	Yes	Yes
Colorado	No	No	Yes	Yes	Yes	Yes	Yes	Yes
Connecticut	Yes	No	Yes	Yes	Yes	No	No	No
Delaware	Yes	Yes	Yes	Yes	Yes	No	No	No
Florida	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Georgia	Yes	No	Yes	Yes	Yes	No	No	No
Hawaii	No	No	Yes	Yes	Yes	No	No	No
Idaho	No	No	Yes	Yes	Yes	Yes	Yes	Yes
Illinois	No	No	Yes	Yes	Yes	Yes	Yes	No
Indiana	No	No	Yes	Yes	Yes	Yes	Yes	No
Iowa	Yes	Yes	Yes	Yes	Yes	Yes	Yes	No
Kansas	No	No	Yes	Yes	Yes	No	Yes	No
Kentucky	Yes	Yes	Yes	Yes	Yes	No	Yes	No
Louisiana	No	No	Yes	Yes	Yes	No	No	Yes
Maine	Yes	No	Yes	Yes	Yes	Yes	Yes	No
Maryland	Yes	No	Yes	Yes	Yes	No	No	No
Massachusetts	No	No	Yes	Yes	Yes	Yes	Yes	Yes
Michigan	No	No	Yes	Yes	Yes	Yes	Yes	Yes
Minnesota	Yes	No	Yes	Yes	Yes	Yes	Yes	Yes
Mississippi	Yes	Yes	Yes	Yes	Yes	No	No	No
Missouri	Yes	Yes	Yes	Yes	Yes	No	Yes	No
Montana	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Nebraska	No	No	Yes	Yes	Yes	No	Yes	Yes
Nevada	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
New Hampshire	No	No	Yes	Yes	No	Yes	No	Yes
New Jersey	Yes	No	Yes	Yes	Yes	No	Yes	No
New Mexico	Yes	No	Yes	Yes	Yes	No	Yes	Yes
New York	No	No	Yes	Yes	Yes	No	No	No
North Carolina	Yes	No	Yes	Yes	Yes	No	No	Yes
North Dakota	Yes	No	Yes	Yes	Yes	Yes	Yes	Yes
Ohio	Yes	No	Yes	Yes	Yes	No	No	Yes
Oklahoma	Yes	No	Yes	Yes	Yes	No	Yes	No
Oregon	No	No	Yes	Yes	Yes	Yes	Yes	Yes
Pennsylvania	No	No	Yes	Yes	Yes	Yes	Yes	Yes
Rhode Island	Yes	No	Yes	Yes	Yes	Yes	Yes	Yes
South Carolina	Yes	No	Yes	Yes	Yes	Yes	Yes	Yes
South Dakota	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Tennessee	No	No	Yes	Yes	No	Yes	Yes	No
Texas	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Utah	No	No	Yes	Yes	Yes	Yes	Yes	Yes
Vermont	Yes	No	Yes	Yes	Yes	Yes	Yes	Yes
Virginia	No	No	Yes	Yes	Yes	No	No	No
Washington	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
West Virginia	Yes	No	Yes	Yes	Yes	No	No	No
Wisconsin	Yes	No	Yes	Yes	Yes	Yes	Yes	No
Wyoming	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
District of Columbia	Yes	Yes	Yes	Yes	Yes	No	Yes	Yes

**Sources:** CCH, Tax Foundation.

*Table 14*  
*Other Individual Income Tax Base Criteria*  
*As of July 1, 2008*

State	Federal Income Used as State Tax Base	State Tax Deductible	AMT Levied	Recognition of LLC Status	Recognition of S-Corp Status
Alabama	No	Yes	No	Yes	Yes
Alaska	n.a.	n.a.	n.a.	Yes	Yes
Arizona	Yes	Yes	No	Yes	Yes
Arkansas	No	Yes	No	Yes	Yes
California	Yes	Yes	Yes	Yes	Partial
Colorado	Yes	Yes	Yes	Yes	Yes
Connecticut	Yes	Yes	Yes	Yes	Yes
Delaware	Yes	Yes	No	Yes	Yes
Florida	n.a.	n.a.	n.a.	Yes	Yes
Georgia	Yes	Yes	No	Yes	Yes
Hawaii	Yes	Yes	No	Yes	Yes
Idaho	Yes	Yes	No	Yes	Yes
Illinois	Yes	Yes	No	Yes	Partial
Indiana	Yes	Yes	No	Yes	Yes
Iowa	No	Yes	Yes	Yes	Yes
Kansas	Yes	Yes	No	Yes	Yes
Kentucky	Yes	Yes	No	Yes	Yes
Louisiana	Yes	Yes	No	Yes	No
Maine	Yes	Yes	Yes	Yes	Yes
Maryland	Yes	Yes	Yes	Yes	Yes
Massachusetts	Yes	Yes	No	Yes	Partial
Michigan	Yes	Yes	No	Yes	No
Minnesota	Yes	Yes	Yes	Yes	Yes
Mississippi	No	Yes	No	Yes	Yes
Missouri	Yes	Yes	No	Yes	Yes
Montana	Yes	Yes	No	Yes	Yes
Nebraska	Yes	Yes	Yes	Yes	Yes
Nevada	n.a.	n.a.	n.a.	n.a.	n.a.
New Hampshire	No	Yes	No	Partial	No
New Jersey	No	Yes	No	Partial	Yes
New Mexico	Yes	Yes	No	Yes	Yes
New York	Yes	Yes	Yes	Yes	Partial
North Carolina	Yes	Yes	No	Yes	Yes
North Dakota	Yes	Yes	No	Yes	Yes
Ohio	Yes	Yes	No	Partial	Yes
Oklahoma	Yes	Yes	No	Yes	Yes
Oregon	Yes	Yes	No	Yes	Yes
Pennsylvania	No	Yes	No	Yes	Yes
Rhode Island	Yes	Yes	Yes	Yes	Partial
South Carolina	Yes	Yes	No	Yes	Yes
South Dakota	n.a.	n.a.	n.a.	n.a.	n.a.
Tennessee	No	Yes	No	Yes	No
Texas	n.a.	n.a.	n.a.	No	No
Utah	Yes	Yes	No	Yes	Yes
Vermont	Yes	Yes	No	Yes	Yes
Virginia	Yes	Yes	No	Partial	Yes
Washington	n.a.	n.a.	n.a.	Yes	Yes
West Virginia	Yes	Yes	Yes	Yes	Yes
Wisconsin	Yes	Yes	Yes	Yes	Yes
Wyoming	n.a.	n.a.	n.a.	n.a.	n.a.
District of Columbia	Yes	Yes	No	Yes	No

**Sources:** CCH, Tax Foundation.



*Table 15*  
*Sales and Excise Tax Rates*  
*As of July 1, 2008*

State	State Sales Tax Rate	County and City Sales Tax		Selective Sales Taxes (Excise Taxes)				
		Weighted Average Rate	Are Localities Permitted to Define Tax Base?	Gasoline Tax (per gallon)	Diesel Tax (per gallon)	Cigarette Tax (per pack of 20)	Beer Tax (per gallon)	Spirits Tax (per gallon)
Alabama	4%	3.15%	No	21.2¢	22.2¢	42.5¢	71¢	\$ 14.78 (a)
Alaska	None	0.86%	No	8¢	8¢	200¢	107¢	\$ 12.80
Arizona	5.6%	2.17%	No	19¢	28¢	200¢	16¢	\$ 3.00
Arkansas	6%	1.36%	No	21.8¢	22.8¢	59¢	24¢	\$ 2.50
California	6.25%	1.71%	No	19.2¢	19.2¢	87¢	20¢	\$ 3.30
Colorado	2.9%	1.85%	Yes	22¢	20.5¢	84¢	8¢	\$ 2.28
Connecticut	6%	None	No	25¢	43.4¢	200¢	19¢	\$ 4.50
Delaware	None	None	No	23¢	22¢	115¢	16¢	\$ 5.46
Florida	6%	0.63%	No	33.2¢	29¢	33.9¢	48¢	\$ 6.50
Georgia	4%	2.76%	No	7.5¢	7.5¢	37¢	101¢	\$ 3.79
Hawaii	4%	0.38%	No	32.6¢	32.6¢	180¢	93¢	\$ 5.98
Idaho	6%	None	Yes	25¢	25¢	57¢	45¢	\$ 8.86 (a)
Illinois	6.25%	1.70%	No	20.9¢	23.4¢	98¢	19¢	\$ 4.50
Indiana	7%	None	No	19¢	28¢	99.5¢	12¢	\$ 2.68
Iowa	6%	0.66%	No	22¢	23.5¢	136¢	19¢	\$ 10.79 (a)
Kansas	5.3%	1.39%	No	25¢	27¢	79¢	18¢	\$ 2.50
Kentucky	6%	None	No	22.5¢	19.5¢	30¢	10¢	\$ 1.94
Louisiana	4%	4.16%	No	20¢	20¢	36¢	32¢	\$ 2.50
Maine	5%	None	No	29.9¢	30.3¢	200¢	35¢	\$ 4.56 (a)
Maryland	6%	None	No	23.5¢	24.3¢	200¢	9¢	\$ 1.50
Massachusetts	5%	None	No	23.5¢	23.5¢	251¢	11¢	\$ 4.05
Michigan	6%	None	No	19.9¢	15.9¢	200¢	20¢	\$ 10.57 (a)
Minnesota	6.5%	0.28%	No	22¢	22¢	150.4¢	15¢	\$ 5.03
Mississippi	7%	None	No	18.8¢	18.8¢	18¢	43¢	\$ 6.34 (a)
Missouri	4.23%	3.22%	No	17.6¢	17.6¢	17¢	6¢	\$ 2.00
Montana	None	None	No	27.8¢	28.6¢	170¢	14¢	\$ 7.26 (a)
Nebraska	5.5%	1.39%	No	26.9¢	26.3¢	64¢	31¢	\$ 3.75
Nevada	6.5%	1.06%	No	32.6¢	28.6¢	80¢	16¢	\$ 3.60
New Hampshire	None	None	No	19.6¢	19.6¢	108¢	30¢	(a)
New Jersey	7%	None	No	14.5¢	17.5¢	257.5¢	12¢	\$ 4.40
New Mexico	5%	1.63%	No	18¢	19¢	91¢	41¢	\$ 6.06
New York	4%	4.25%	Yes	33.2¢	31.4¢	275¢	11¢	\$ 6.44
North Carolina	4.25%	2.58%	No	30.2¢	30.2¢	35¢	53¢	\$ 8.98 (a)
North Dakota	5%	1.33%	No	23¢	23¢	44¢	16¢	\$ 2.50
Ohio	5.5%	1.27%	No	28¢	28¢	125¢	18¢	\$ 8.40 (a)
Oklahoma	4.5%	2.42%	No	17¢	14¢	103¢	40¢	\$ 5.56
Oregon	None	None	No	25¢	24.3¢	118¢	8¢	\$ 18.52 (a)
Pennsylvania	6%	0.22%	No	32.3¢	39.2¢	135¢	8¢	\$ 6.54 (a)
Rhode Island	7%	None	No	31¢	31¢	246¢	11¢	\$ 3.75
South Carolina	6%	0.84%	No	16.8¢	16.8¢	7¢	84¢	\$ 5.42
South Dakota	4%	2%	No	22¢	24¢	153¢	27¢	\$ 3.93
Tennessee	7%	2.36%	No	21.4¢	18.4¢	62¢	14¢	\$ 4.40
Texas	6.25%	0.44%	No	20¢	20¢	141¢	20¢	\$ 2.40
Utah	4.65%	1.89%	No	24.5¢	24.5¢	69.5¢	41¢	\$ 9.66 (a)
Vermont	6%	0.28%	No	20¢	26¢	199¢	27¢	\$ 0.38 (a)
Virginia	4%	1%	No	18.1¢	19.6¢	30¢	26¢	\$ 14.54 (a)
Washington	6.5%	2.12%	No	37.5¢	37.5¢	202.5¢	26¢	\$ 21.30 (a)
West Virginia	6%	None	No	32.2¢	32.2¢	55¢	18¢	\$ 1.70 (a)
Wisconsin	5%	0.41%	No	32.9¢	32.9¢	177¢	6¢	\$ 3.25
Wyoming	4%	1.47%	No	14¢	14¢	60¢	2¢	(a)
District of Columbia	5.75%	None	No	20¢	20¢	100¢	9¢	\$ 1.50

(a) Eighteen states outlaw private liquor sales and set up state-run stores. These are called "control states" while "license states" are those that permit private wholesale and retail sales. All license states have an excise tax rate in law, expressed in dollars per gallon. Control states levy no statutory tax but usually raise comparable revenue by charging higher prices. Since July 2005, the Distilled Spirits Council of the U.S., a trade association, has computed approximate excise tax rates for control states by comparing prices of typical products sold in their state-run stores to the pre-tax prices of liquor in states where liquor is privately sold. In New Hampshire and Wyoming, average liquor prices charged in state-run stores are lower than pre-tax prices in license states.

Sources: CCH, American Petroleum Institute, Distilled Spirits Council of the U.S., and Tax Foundation.

*Table 16*  
*State Sales Tax Exemptions for Business-to-Business Transactions*  
*As of July 1, 2008*

State	Insecticides and Pesticides	Fertilizer, Seed and Feed	Seedlings, Plants and Shoots	Manufacturing Machinery	Utilities	Farm Machinery
Alabama	Exempt	Exempt	Exempt	Taxable	Exempt	Taxable
Arizona	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Arkansas	Taxable	Exempt	Exempt	Exempt	Taxable	Exempt
California	Taxable	Exempt	Exempt	Taxable	Exempt	Taxable
Colorado	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Connecticut	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Florida	Exempt	Exempt	Exempt	Taxable	Exempt	Exempt
Georgia	Exempt	Exempt	Exempt	Exempt	Taxable	Exempt
Hawaii	Taxable	Taxable	Taxable	Taxable	Taxable	Taxable
Idaho	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Illinois	Exempt	Exempt	Exempt	Exempt	Taxable	Exempt
Indiana	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Iowa	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Kansas	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Kentucky	Exempt	Exempt	Exempt	Taxable	Exempt	Exempt
Louisiana	Exempt	Exempt	Exempt	Taxable	Taxable	Taxable
Maine	Exempt	Exempt	Exempt	Exempt	Taxable	Exempt
Maryland	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Massachusetts	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Michigan	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Minnesota	Exempt	Exempt	Exempt	Taxable	Exempt	Exempt
Mississippi	Exempt	Exempt	Exempt	Taxable	Taxable	Taxable
Missouri	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Nebraska	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Nevada	Taxable	Exempt	Exempt	Taxable	Taxable	Taxable
New Jersey	Exempt	Exempt	Exempt	Exempt	Taxable	Exempt
New Mexico	Exempt	Exempt	Exempt	Taxable	Taxable	Taxable
New York	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
North Carolina	Exempt	Exempt	Exempt	Taxable	Taxable	Taxable
North Dakota	Exempt	Exempt	Exempt	Taxable	Taxable	Taxable
Ohio	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Oklahoma	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Pennsylvania	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Rhode Island	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
South Carolina	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
South Dakota	Exempt	Exempt	Exempt	Taxable	Taxable	Taxable
Tennessee	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Texas	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Utah	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Vermont	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Virginia	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Washington	Exempt	Exempt	Exempt	Exempt	Taxable	Taxable
West Virginia	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Wisconsin	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Wyoming	Taxable	Exempt	Exempt	Exempt	Exempt	Taxable
District of Columbia	Taxable	Taxable	Taxable	Taxable	Exempt	Taxable

Note: States with no state sales tax omitted from table: Alaska, Delaware, Montana, New Hampshire and Oregon.  
Sources: CCH, Tax Foundation.

*Table 16 (continued)*  
*State Sales Tax Exemptions for Business-to-Business Transactions*  
*As of July 1, 2008*

State	General Treatment of Services	Cleaning Services	Transportation Services	Repair Services	Professional and Personal Services	Custom Software
Alabama	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Arizona	Many Taxable	Exempt	Taxable	Exempt	Exempt	Exempt
Arkansas	Many Taxable	Taxable	Exempt	Taxable	Exempt	Taxable
California	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Colorado	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Connecticut	Many Taxable	Taxable	Exempt	Taxable	Taxable	Taxable
Florida	Many Taxable	Taxable	Exempt	Exempt	Exempt	Exempt
Georgia	Exempt	Exempt	Taxable	Exempt	Exempt	Exempt
Hawaii	Generally Taxable	Taxable	Taxable	Taxable	Taxable	Taxable
Idaho	Exempt	Exempt	Taxable	Exempt	Exempt	Exempt
Illinois	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Indiana	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Iowa	Many Taxable	Taxable	Exempt	Taxable	Taxable	Exempt
Kansas	Many Taxable	Exempt	Exempt	Taxable	Exempt	Exempt
Kentucky	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Louisiana	Exempt	Exempt	Exempt	Taxable	Exempt	Exempt
Maine	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Maryland	Exempt	Taxable	Exempt	Exempt	Exempt	Exempt
Massachusetts	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Michigan	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Minnesota	Many Taxable	Taxable	Exempt	Exempt	Exempt	Exempt
Mississippi	Generally Taxable	Exempt	Exempt	Taxable	Exempt	Taxable
Missouri	Exempt	Exempt	Taxable	Exempt	Exempt	Exempt
Nebraska	Exempt	Taxable	Exempt	Taxable	Exempt	Taxable
Nevada	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
New Jersey	Many Taxable	Taxable	Exempt	Taxable	Exempt	Exempt
New Mexico	Generally Taxable	Taxable	Taxable	Taxable	Taxable	Taxable
New York	Many Taxable	Taxable	Exempt	Taxable	Exempt	Exempt
North Carolina	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
North Dakota	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Ohio	Many Taxable	Taxable	Taxable	Taxable	Exempt	Taxable
Oklahoma	Many Taxable	Exempt	Taxable	Exempt	Exempt	Exempt
Pennsylvania	Many Taxable	Taxable	Exempt	Taxable	Exempt	Exempt
Rhode Island	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
South Carolina	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
South Dakota	Generally Taxable	Taxable	Taxable	Taxable	Taxable	Taxable
Tennessee	Exempt	Exempt	Exempt	Taxable	Exempt	Taxable
Texas	Many Taxable	Taxable	Exempt	Taxable	Taxable	Taxable
Utah	Many Taxable	Exempt	Taxable	Taxable	Exempt	Exempt
Vermont	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Virginia	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Washington	Many Taxable	Exempt	Exempt	Taxable	Exempt	Exempt
West Virginia	Generally Taxable	Taxable	Taxable	Taxable	Exempt	Taxable
Wisconsin	Many Taxable	Exempt	Exempt	Taxable	Exempt	Exempt
Wyoming	Exempt	Exempt	Taxable	Taxable	Exempt	Exempt
District of Columbia	Many Taxable	Taxable	Exempt	Taxable	Exempt	Taxable

Note: States with no state sales tax omitted from table: Alaska, Delaware, Montana, New Hampshire and Oregon.

Source: CCH.

*Table 16 (continued)*  
*State Sales Tax Exemptions for Business-to-Business Transactions*  
*As of July 1, 2008*

State	Modified Canned Software	Downloaded Software	Leasing Motor Vehicles	Leasing Tangible Personal Property	Leasing Rooms and Lodgings
Alabama	Taxable	Taxable	Taxable	Taxable	Taxable
Arizona	Taxable	Taxable	Taxable	Taxable	Taxable
Arkansas	Taxable	Exempt	Taxable	Taxable	Taxable
California	Taxable	Exempt	Taxable	Taxable	Exempt
Colorado	Exempt	Exempt	Taxable	Taxable	Taxable
Connecticut	Taxable	Taxable	Taxable	Taxable	Taxable
Florida	Exempt	Exempt	Taxable	Taxable	Taxable
Georgia	Taxable	Exempt	Taxable	Taxable	Taxable
Hawaii	Taxable	Taxable	Taxable	Taxable	Taxable
Idaho	Taxable	Taxable	Taxable	Taxable	Taxable
Illinois	Exempt	Taxable	Taxable	Exempt	Taxable
Indiana	Taxable	Taxable	Taxable	Taxable	Taxable
Iowa	Taxable	Exempt	Taxable	Taxable	Taxable
Kansas	Taxable	Taxable	Taxable	Taxable	Taxable
Kentucky	Exempt	Taxable	Exempt	Taxable	Taxable
Louisiana	Taxable	Taxable	Taxable	Taxable	Taxable
Maine	Taxable	Taxable	Taxable	Taxable	Taxable
Maryland	Exempt	Exempt	Taxable	Taxable	Taxable
Massachusetts	Exempt	Taxable	Taxable	Taxable	Taxable
Michigan	Taxable	Taxable	Taxable	Taxable	Taxable
Minnesota	Taxable	Taxable	Taxable	Taxable	Taxable
Mississippi	Taxable	Taxable	Taxable	Taxable	Taxable
Missouri	Taxable	Exempt	Taxable	Taxable	Taxable
Nebraska	Taxable	Taxable	Taxable	Taxable	Taxable
Nevada	Taxable	Exempt	Taxable	Taxable	Exempt
New Jersey	Taxable	Exempt	Taxable	Taxable	Taxable
New Mexico	Taxable	Taxable	Taxable	Taxable	Taxable
New York	Taxable	Taxable	Taxable	Taxable	Taxable
North Carolina	Taxable	Exempt	Exempt	Taxable	Taxable
North Dakota	Taxable	Taxable	Exempt	Taxable	Taxable
Ohio	Taxable	Taxable	Taxable	Taxable (a)	Taxable
Oklahoma	Taxable	Exempt	Taxable	Taxable	Taxable
Pennsylvania	Taxable	Taxable	Taxable	Taxable	Taxable
Rhode Island	Taxable	Exempt	Taxable	Taxable	Taxable
South Carolina	Taxable	Exempt	Taxable	Taxable	Taxable
South Dakota	Taxable	Taxable	Taxable	Taxable	Taxable
Tennessee	Taxable	Taxable	Taxable	Taxable	Taxable
Texas	Taxable	Taxable	Exempt	Taxable	Taxable
Utah	Taxable	Taxable	Taxable	Taxable	Taxable
Vermont	Exempt	Exempt	Exempt	Taxable	Taxable
Virginia	Taxable	Exempt	Exempt	Taxable	Taxable
Washington	Exempt	Taxable	Taxable	Taxable	Taxable
West Virginia	Taxable	Taxable	Taxable	Taxable	Taxable
Wisconsin	Taxable	Taxable	Taxable	Taxable	Taxable
Wyoming	Taxable	Taxable	Taxable	Taxable	Taxable
District of Columbia	Taxable	Taxable	Taxable	Taxable	Taxable

Note: States with no state sales tax omitted from table: Alaska, Delaware, Montana, New Hampshire and Oregon.

(a) Tax phases out completely in 2009. Current score reflects partial phase-out as of July 1, 2008.

Source: CCH.



*Table 16 (continued)*  
*State Sales Tax Exemptions for Business-to-Business Transactions*  
*As of July 1, 2008*

State	Raw Material	Office Equipment	Pollution Control Equipment	
			Air	Water
Alabama	Exempt	Taxable	Exempt	Exempt
Arizona	Exempt	Taxable	Exempt	Exempt
Arkansas	Exempt	Taxable	Exempt	Exempt
California	Exempt	Taxable	Taxable	Taxable
Colorado	Exempt	Taxable	Taxable	Taxable
Connecticut	Exempt	Taxable	Exempt	Exempt
Florida	Exempt	Taxable	Exempt	Exempt
Georgia	Exempt	Taxable	Exempt	Exempt
Hawaii	Taxable	Taxable	Exempt	Taxable
Idaho	Exempt	Taxable	Exempt	Exempt
Illinois	Exempt	Taxable	Taxable	Taxable
Indiana	Exempt	Taxable	Exempt	Exempt
Iowa	Exempt	Taxable	Exempt	Exempt
Kansas	Exempt	Taxable	Exempt	Exempt
Kentucky	Exempt	Taxable	Exempt	Exempt
Louisiana	Exempt	Taxable	Exempt	Exempt
Maine	Exempt	Taxable	Exempt	Exempt
Maryland	Exempt	Taxable	Exempt	Exempt
Massachusetts	Exempt	Taxable	Taxable	Taxable
Michigan	Exempt	Taxable	Exempt	Exempt
Minnesota	Exempt	Taxable	Taxable	Taxable
Mississippi	Exempt	Taxable	Exempt	Exempt
Missouri	Exempt	Taxable	Exempt	Exempt
Nebraska	Exempt	Taxable	Taxable	Taxable
Nevada	Exempt	Taxable	Taxable	Taxable
New Jersey	Exempt	Taxable	Taxable	Taxable
New Mexico	Exempt	Taxable	Taxable	Taxable
New York	Exempt	Taxable	Exempt	Exempt
North Carolina	Exempt	Taxable	Taxable	Taxable
North Dakota	Exempt	Taxable	Taxable	Taxable
Ohio	Exempt	Taxable	Exempt	Exempt
Oklahoma	Exempt	Taxable	Taxable	Taxable
Pennsylvania	Exempt	Taxable	Exempt	Exempt
Rhode Island	Exempt	Taxable	Exempt	Exempt
South Carolina	Exempt	Taxable	Exempt	Exempt
South Dakota	Exempt	Taxable	Taxable	Taxable
Tennessee	Exempt	Taxable	Exempt	Exempt
Texas	Exempt	Taxable	Exempt	Exempt
Utah	Exempt	Taxable	Exempt	Exempt
Vermont	Exempt	Taxable	Taxable	Taxable
Virginia	Exempt	Taxable	Exempt	Exempt
Washington	Exempt	Taxable	Taxable	Taxable
West Virginia	Exempt	Taxable	Exempt	Exempt
Wisconsin	Exempt	Taxable	Taxable	Taxable
Wyoming	Exempt	Taxable	Taxable	Taxable
District of Columbia	Exempt	Taxable	Taxable	Taxable

Note: States with no state sales tax omitted from table: Alaska, Delaware, Montana, New Hampshire and Oregon.  
Sources: CCH.

*Table 17*  
*State Sales Tax Exemptions for*  
*Business-to-Consumer Transactions*  
*As of July 1, 2008*

State	Gasoline Exemption	Grocery Exemption
Alabama	Exempt	Taxable
Arizona	Exempt	Exempt
Arkansas	Exempt	Partial
California	Taxable	Exempt
Colorado	Partial	Exempt
Connecticut	Exempt	Exempt
Florida	Exempt	Exempt
Georgia	Partial	Exempt
Hawaii	Exempt	Taxable
Idaho	Exempt	Taxable
Illinois	Taxable	Partial
Indiana	Taxable	Exempt
Iowa	Exempt	Exempt
Kansas	Exempt	Taxable
Kentucky	Exempt	Exempt
Louisiana	Exempt	Exempt
Maine	Exempt	Exempt
Maryland	Exempt	Exempt
Massachusetts	Exempt	Exempt
Michigan	Taxable	Exempt
Minnesota	Exempt	Exempt
Mississippi	Exempt	Taxable
Missouri	Exempt	Partial
Nebraska	Exempt	Exempt
Nevada	Exempt	Exempt
New Jersey	Exempt	Exempt
New Mexico	Exempt	Exempt
New York	Partial	Exempt
North Carolina	Exempt	Exempt
North Dakota	Exempt	Exempt
Ohio	Exempt	Exempt
Oklahoma	Exempt	Taxable
Pennsylvania	Exempt	Exempt
Rhode Island	Exempt	Exempt
South Carolina	Exempt	Taxable
South Dakota	Exempt	Taxable
Tennessee	Exempt	Partial
Texas	Exempt	Exempt
Utah	Exempt	Partial
Vermont	Exempt	Exempt
Virginia	Exempt	Partial
Washington	Exempt	Exempt
West Virginia	Exempt	Partial
Wisconsin	Exempt	Exempt
Wyoming	Exempt	Exempt
District of Columbia	Exempt	Exempt

Note: States with no state sales tax omitted from table: Alaska, Delaware, Montana, New Hampshire and Oregon.  
Sources: CCH, Tax Foundation, American Petroleum Institute.

*Table 18*  
*State Unemployment Insurance Tax Rates*

State	Rates in Effect on July 1, 2008			Most Favorable Schedule		Least Favorable Schedule	
	Minimum Rate	Maximum Rate	Taxable Wage Threshold	Minimum Rate	Maximum Rate	Minimum Rate	Maximum Rate
Alabama	0.44%	6.04%	\$8,000	0.20%	5.40%	0.65%	6.80%
Alaska	1.00%	5.40%	\$30,300	None	5.40%	1.00%	5.40%
Arizona	0.02%	5.40%	\$7,000	0.02%	5.40%	0.10%	5.40%
Arkansas	0.10%	10.00%	\$10,000	None	5.90%	0.90%	10.80%
California	None	5.40%	\$7,000	0.10%	5.40%	1.50%	6.20%
Colorado	0.30%	5.40%	\$10,000	None	5.40%	1.00%	5.40%
Connecticut	0.50%	5.40%	\$15,000	0.50%	5.40%	1.90%	6.80%
Delaware	0.30%	8.20%	\$10,500	0.10%	8.00%	0.10%	8.00%
Florida	0.10%	5.40%	\$7,000	0.10%	5.40%	0.10%	5.40%
Georgia	0.03%	5.40%	\$8,500	0.01%	5.40%	0.03%	7.29%
Hawaii	None	5.40%	\$13,000	None	5.40%	2.40%	5.40%
Idaho	0.26%	5.40%	\$32,200	0.18%	5.40%	0.96%	6.80%
Illinois	0.20%	7.20%	\$12,000	0.20%	6.40%	0.30%	9.60%
Indiana	1.10%	5.60%	\$7,000	0.10%	5.40%	1.10%	5.60%
Iowa	None	8.00%	\$22,800	None	7.00%	None	9.00%
Kansas	None	7.40%	\$8,000	0.01%	7.40%	0.01%	7.40%
Kentucky	0.60%	9.75%	\$8,000	0.30%	9.00%	1.00%	10.00%
Louisiana	0.10%	6.20%	\$7,000	0.09%	6.00%	0.30%	6.00%
Maine	0.42%	5.40%	\$12,000	0.42%	5.40%	1.03%	8.83%
Maryland	0.30%	7.50%	\$8,500	0.30%	7.50%	2.20%	13.50%
Massachusetts	1.12%	10.96%	\$14,000	0.80%	7.80%	1.58%	15.40%
Michigan	0.06%	10.30%	\$9,000	0.06%	10.30%	0.06%	10.30%
Minnesota	0.40%	9.30%	\$25,000	0.10%	9.00%	0.40%	9.30%
Mississippi	0.40%	5.40%	\$7,000	0.10%	5.40%	0.10%	5.40%
Missouri	None	6.00%	\$12,000	None	5.40%	None	7.80%
Montana	None	6.12%	\$23,800	None	6.12%	1.62%	6.12%
Nebraska	None	5.40%	\$9,000	None	5.40%	None	5.40%
Nevada	0.25%	5.40%	\$25,400	0.25%	5.40%	0.25%	5.40%
New Hampshire	0.10%	6.50%	\$8,000	0.10%	6.50%	0.10%	6.30%
New Jersey	0.18%	5.40%	\$27,700	0.18%	5.40%	1.18%	7.70%
New Mexico	0.03%	5.40%	\$19,900	0.02%	5.40%	2.70%	5.40%
New York	0.50%	8.90%	\$8,500	None	5.90%	0.90%	8.90%
North Carolina	None	5.70%	\$18,600	None	5.70%	None	5.70%
North Dakota	0.34%	9.86%	\$22,100	0.20%	8.09%	0.49%	10.09%
Ohio	0.40%	9.20%	\$9,000	None	6.30%	0.30%	8.90%
Oklahoma	0.10%	5.50%	\$13,600	0.20%	5.50%	0.50%	5.50%
Oregon	0.70%	5.40%	\$30,200	0.50%	5.40%	2.20%	5.40%
Pennsylvania	0.30%	9.20%	\$8,000	0.30%	7.70%	0.30%	7.70%
Rhode Island	1.69%	9.79%	\$14,000	0.60%	7.00%	1.90%	10.00%
South Carolina	0.54%	5.40%	\$7,000	0.54%	5.40%	1.24%	6.10%
South Dakota	None	8.50%	\$9,000	None	8.50%	1.50%	10.00%
Tennessee	0.30%	10.00%	\$7,000	None	10.00%	0.50%	10.00%
Texas	0.10%	6.10%	\$9,000	None	6.00%	None	6.00%
Utah	0.10%	9.10%	\$26,700	None	9.00%	None	9.00%
Vermont	1.10%	7.70%	\$8,000	0.40%	5.40%	1.30%	8.40%
Virginia	0.10%	6.20%	\$8,000	None	5.40%	0.10%	6.20%
Washington	0.38%	6.02%	\$34,000	None	5.40%	None	5.40%
West Virginia	1.50%	7.50%	\$8,000	None	8.50%	1.50%	8.50%
Wisconsin	None	8.90%	\$10,500	None	8.90%	0.27%	8.90%
Wyoming	0.27%	9.03%	\$20,100	None	10.00%	None	10.00%
District of Columbia	1.30%	6.60%	\$9,000	0.10%	5.40%	1.90%	7.40%

Source: U.S. Department of Labor.

**Table 19**  
**State Unemployment Insurance Tax Base Criteria**  
**As of January 1, 2008**

		Benefits are Charged to Employers in Proportion to Base Period Wages	Company Charged for Benefits If					Employee Continues to Work for Employer Part-time
State	State Experience Formula		Employee's Benefit Award Reversed	Reimbursements on Combined Wage Claims	Employee Left Voluntarily	Employee Discharged for Misconduct	Employee Refused Suitable Work	
Alabama	Benefit-Ratio	Yes	No	Yes	No	No	Yes	No
Alaska	Payroll Variation	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Arizona	Reserve-Ratio	Yes	No	No	No	No	Yes	No
Arkansas	Reserve-Ratio	Yes	Yes	Yes	No	No	Yes	No
California	Reserve-Ratio	Yes	No	Yes	No	No	Yes	No
Colorado	Reserve-Ratio	No (b)	No	No	No	No	Yes	Yes
Connecticut	Benefit-Ratio	Yes	Yes	Yes	No	No	No	Yes
Delaware	State Experience	Yes	No	No	No	No	Yes	No
Florida	Benefit-Ratio	Yes	No	Yes	No	No	No	Yes
Georgia	Reserve-Ratio	No (a)	No	No	No	No	No	Yes
Hawaii	Reserve-Ratio	Yes	Yes	No	No	No	Yes	No
Idaho	Reserve-Ratio	No (a)	No	No	No	No	Yes	Yes
Illinois	Benefit-Ratio	No (a)	Yes	No	No	No	No	Yes
Indiana	Reserve-Ratio	Yes	Yes	No	No	No	Yes	No
Iowa	Benefit-Ratio	No (b)	No	No	No	No	No	Yes
Kansas	Reserve-Ratio	Yes	Yes	Yes	No	No	Yes	No
Kentucky	Reserve-Ratio	No (a)	Yes	No	No	No	Yes	Yes
Louisiana	Reserve-Ratio	Yes	No	Yes	No	No	No	No
Maine	Reserve-Ratio	No (a)	No	No	No	No	No	No
Maryland	Benefit-Ratio	Yes	No	Yes	No	Yes	Yes	No
Massachusetts	Reserve-Ratio	No (b)	No	Yes	No	Yes	Yes	Yes
Michigan	Benefit-Ratio	No (a)	Yes	Yes	No	No	No	No
Minnesota	Benefit-Ratio	Yes	Yes	No	No	No	Yes	Yes
Mississippi	Benefit-Ratio	Yes	Yes	Yes	No	No	No	No
Missouri	Reserve-Ratio	Yes	No	No	No	No	No	Yes
Montana	Reserve-Ratio	Yes	No	Yes	No	No	Yes	No
Nebraska	Reserve-Ratio	No (b)	No	Yes	No	No	Yes	Yes
Nevada	Reserve-Ratio	No (a)	Yes	No	No	No	Yes	Yes
New Hampshire	Reserve-Ratio	No (a)	Yes	No	Yes	Yes	Yes	Yes
New Jersey	Reserve-Ratio	Yes	No	Yes	No	No	No	Yes
New Mexico	Reserve-Ratio	Yes	No	Yes	No	No	Yes	Yes
New York	Reserve-Ratio	No (a)	Yes	Yes	No	No	Yes	No
North Carolina	Reserve-Ratio	Yes	No	Yes	No	No	Yes	No
North Dakota	Reserve-Ratio	Yes	No	Yes	No	No	Yes	Yes
Ohio	Reserve-Ratio	Yes	No	No	No	No	No	No
Oklahoma	State Experience	Yes	No	Yes	No	No	Yes	No
Oregon	Benefit-Ratio	Yes	No	No	No	No	Yes	No
Pennsylvania	Benefit-Ratio	Yes	No	Yes	No	No	Yes	No
Rhode Island	Reserve-Ratio	No (a)	No	Yes	No	No	Yes	Yes
South Carolina	Reserve-Ratio	No (a)	No	Yes	No	No	No	Yes
South Dakota	Reserve-Ratio	No (b)	No	Yes	No	No	Yes	Yes
Tennessee	Reserve-Ratio	Yes	No	Yes	No	No	Yes	No
Texas	Benefit-Ratio	Yes	No	Yes	No	No	Yes	Yes
Utah	Benefit-Ratio	Yes	No	No	No	No	Yes	No
Vermont	Benefit-Ratio	Yes	Yes	No	No	No	No	No
Virginia	Benefit-Ratio	No (a)	Yes	No	No	Yes	No	Yes
Washington	Benefit-Ratio	No (b)	No	Yes	No	No	Yes	No
West Virginia	Reserve-Ratio	Yes	No	Yes	No	No	Yes	Yes
Wisconsin	Reserve-Ratio	Yes	No	Yes	No	Yes	Yes	Yes
Wyoming	Benefit-Ratio	Yes	No	Yes	No	No	Yes	No
District of Columbia	Reserve-Ratio	Yes	Yes	Yes	No	No	Yes	No

(a) Benefits charged to most recent employer.

(b) Benefits charged to base-period employers, most recent first.

Source: U.S. Department of Labor

*Table 20*  
*Other State Unemployment Insurance Tax Base Criteria*  
*As of January 1, 2008*

State	Solvency Tax	Taxes for Socialized Costs or Negative Balance Employer	Loan and Interest Repayment Surtaxes	Reserve Taxes	Surtaxes for UI Administration or Non-UI Purposes	Temporary Disability Insurance	Voluntary Contributions	Time-Period to Qualify for Experience Rating(Years)
Alabama	No	Yes	Yes	No	Yes	No	No	1
Alaska	Yes	No	No	No	Yes	No	No	1
Arizona	No	No	No	No	Yes	No	Yes	1
Arkansas	No	No	Yes	No	Yes	No	Yes	3
California	No	No	No	No	Yes	Yes	Yes	1
Colorado	Yes	Yes	Yes	No	Yes	No	Yes	1
Connecticut	No	No	Yes	No	No	No	No	1
Delaware	Yes	No	Yes	No	Yes	No	No	2
Florida	No	No	No	No	No	No	No	2.5
Georgia	No	No	No	No	No	No	Yes	3
Hawaii	No	No	No	No	Yes	Yes	No	1
Idaho	No	No	Yes	Yes	Yes	No	No	1
Illinois	Yes	No	No	No	No	No	No	3
Indiana	No	No	No	No	Yes	No	Yes	3
Iowa	No	No	Yes	Yes	No	No	No	3
Kansas	No	No	No	No	No	No	Yes	2
Kentucky	No	No	No	No	Yes	No	Yes	3
Louisiana	Yes	Yes	Yes	No	Yes	No	Yes	3
Maine	No	No	Yes	No	Yes	No	Yes	2
Maryland	No	No	No	No	No	No	No	2
Massachusetts	No	No	Yes	No	Yes	No	Yes	1
Michigan	No	No	No	No	No	No	Yes	2
Minnesota	Yes	No	Yes	No	Yes	No	Yes	1
Mississippi	No	No	No	No	Yes	No	No	1
Missouri	No	No	Yes	No	No	No	Yes	1
Montana	No	No	No	No	Yes	No	No	3
Nebraska	Yes	No	No	Yes	No	No	Yes	1
Nevada	No	No	No	No	Yes	No	No	2.5
New Hampshire	Yes	No	No	No	Yes	No	No	1
New Jersey	Yes	No	Yes	No	Yes	Yes	Yes	3
New Mexico	No	No	No	Yes	No	No	Yes	3
New York	Yes	No	Yes	No	Yes	Yes	Yes	1
North Carolina	No	No	No	Yes	No	No	Yes	2
North Dakota	Yes	No	No	No	No	No	Yes	3
Ohio	No	Yes	No	No	No	No	Yes	1
Oklahoma	Yes	No	No	No	No	No	No	1
Oregon	No	No	Yes	No	Yes	No	No	1
Pennsylvania	Yes	Yes	Yes	No	No	No	Yes	1.5
Rhode Island	Yes	No	No	No	Yes	Yes	No	3
South Carolina	No	No	No	No	Yes	No	No	2
South Dakota	No	No	No	No	Yes	No	Yes	2
Tennessee	No	No	Yes	No	Yes	No	No	3
Texas	Yes	Yes	Yes	No	Yes	No	Yes	1
Utah	No	Yes	No	No	No	No	No	1
Vermont	No	No	No	No	No	No	No	1
Virginia	Yes	Yes	No	No	No	No	No	1
Washington	Yes	Yes	Yes	No	Yes	No	Yes	2
West Virginia	No	No	Yes	No	No	No	Yes	3
Wisconsin	No	Yes	Yes	No	Yes	No	Yes	1.5
Wyoming	No	No	No	No	Yes	No	No	3
District of Columbia	No	No	No	No	Yes	No	No	3

Source: U.S. Department of Labor



*Table 21*  
*Property Tax Rates and Capital Stock Taxes*  
*As of July 1, 2008*

State	Property Tax Collections Per Capita	Property Tax Collections as a Percentage of Income	Capital Stock Tax Rate	Capital Stock Maximum Payment	Payment Options for CST and CIT
Alabama	\$477	1.31%	0.175%	\$15,000	Pay both
Alaska	\$1,582	3.70%	None	n.a.	n.a.
Arizona	\$993	2.72%	None	n.a.	n.a.
Arkansas	\$527	1.63%	0.300%	Unlimited	Pay both
California	\$1,170	2.57%	None	n.a.	n.a.
Colorado	\$1,205	2.67%	None	n.a.	n.a.
Connecticut	\$2,393	4.13%	0.310%	\$1,000,000	Pay highest
Delaware	\$696	1.53%	0.025%	\$165,000	Pay both
Florida	\$1,361	3.23%	None	n.a.	n.a.
Georgia	\$1,072	2.92%	0.100%	\$5,000	Pay both
Hawaii	\$925	2.18%	None	n.a.	n.a.
Idaho	\$908	2.62%	None	n.a.	n.a.
Illinois	\$1,697	3.85%	0.100%	\$2,000,000	Pay both
Indiana	\$780	2.08%	None	n.a.	n.a.
Iowa	\$1,243	3.23%	None	n.a.	n.a.
Kansas	\$1,315	3.27%	0.094%	\$20,000	Pay both
Kentucky	\$620	1.83%	None	n.a.	n.a.
Louisiana	\$699	1.97%	0.300%	Unlimited	Pay both
Maine	\$1,785	4.71%	None	n.a.	n.a.
Maryland	\$1,175	2.26%	None	n.a.	n.a.
Massachusetts	\$1,864	3.50%	0.260%	Unlimited	Pay both
Michigan	\$1,466	3.77%	None	n.a.	n.a.
Minnesota	\$1,183	2.63%	None	n.a.	n.a.
Mississippi	\$808	2.63%	0.250%	Unlimited	Pay both
Missouri	\$908	2.41%	0.033%	Unlimited	Pay both
Montana	\$1,192	3.34%	None	n.a.	n.a.
Nebraska	\$1,394	3.49%	0.020%	\$15,000	Pay both
Nevada	\$1,157	2.67%	None	n.a.	n.a.
New Hampshire	\$2,320	5.05%	None	n.a.	n.a.
New Jersey	\$2,642	4.88%	None	n.a.	n.a.
New Mexico	\$539	1.55%	None	n.a.	n.a.
New York	\$2,124	4.33%	0.150%	\$10,000,000	Pay highest
North Carolina	\$853	2.32%	0.150%	\$75,000	Pay both
North Dakota	\$1,083	2.87%	None	n.a.	n.a.
Ohio	\$1,339	3.50%	0.160%	\$60,000	Pay highest
Oklahoma	\$562	1.50%	0.125%	\$20,000	Pay both
Oregon	\$1,066	2.75%	None	n.a.	n.a.
Pennsylvania	\$1,255	2.95%	0.289%	Unlimited	Pay both
Rhode Island	\$1,936	4.39%	0.025%	Unlimited	Pay highest
South Carolina	\$1,048	3.10%	0.100%	Unlimited	Pay both
South Dakota	\$1,060	2.70%	None	n.a.	n.a.
Tennessee	\$732	1.98%	0.250%	Unlimited	Pay both
Texas	\$1,441	3.63%	None	n.a.	n.a.
Utah	\$805	2.43%	None	n.a.	n.a.
Vermont	\$2,055	5.12%	None	n.a.	n.a.
Virginia	\$1,381	3.01%	None	n.a.	n.a.
Washington	\$1,174	2.72%	None	n.a.	n.a.
West Virginia	\$623	1.92%	0.550%	Unlimited	Pay both
Wisconsin	\$1,528	3.82%	None	n.a.	n.a.
Wyoming	\$2,175	4.55%	0.020%	Unlimited	Pay both
District of Columbia	\$2,208	3.38%	None	n.a.	n.a.

Source: Census Bureau, CCH, Tax Foundation.

*Table 22*  
*Other Property Tax Base Criteria*  
*As of July 1, 2008*

State	Intangible Property	Inventory	Real Estate Transfer	Estate Tax	Inheritance Tax	Generation- Skipping Transfer Tax	Gift Tax
Alabama	Yes	No	Yes	Copies Federal System	No	No	No
Alaska	No	Yes	No	Copies Federal System	No	No	No
Arizona	No	No	No	Copies Federal System	No	No	No
Arkansas	No	Yes	Yes	Copies Federal System	No	No	No
California	No	No	Yes (b)	Copies Federal System	No	No	No
Colorado	No	No	No (c)	Copies Federal System	No	No	No
Connecticut	No	No	Yes	Decoupled	No	No	Yes
Delaware	No	No	Yes	Copies Federal System	No	No	No
Florida	No	No	Yes	Copies Federal System	No	No	No
Georgia	Yes	Yes	Yes	Copies Federal System	No	No	No
Hawaii	No	No	Yes	Copies Federal System	No	No	No
Idaho	No	No	No	Copies Federal System	No	No	No
Illinois	No	No	Yes	Decoupled	No	No	No
Indiana	No	No	No	Copies Federal System	Yes	No	No
Iowa	Yes	No	Yes	Copies Federal System	Yes	No	No
Kansas	No	No	Yes	Decoupled	No	No	No
Kentucky	No	Yes	Yes	Copies Federal System	Yes	No	No
Louisiana	Yes	Yes	No	Copies Federal System	No	No	No
Maine	No	No	Yes	Decoupled	No	No	No
Maryland	No	Yes	Yes	Decoupled	Yes	No	No
Massachusetts	No	Partial	Yes	Decoupled	No	No	No
Michigan	No	No	Yes	Copies Federal System	No	No	No
Minnesota	No	No	Yes	Copies Federal System	No	No	No
Mississippi	Yes	Yes	No	Copies Federal System	No	No	No
Missouri	No	No	No	Copies Federal System	No	No	No
Montana	No	No	No	Copies Federal System	No	No	No
Nebraska	No	No	Yes	Decoupled	Yes	Yes	No
Nevada	No	No	Yes	Copies Federal System	No	No	No
New Hampshire	No	No	Yes	Copies Federal System	No	No	No
New Jersey	No	No	Yes	Decoupled	Yes	No	No
New Mexico	No	No	No	Copies Federal System	No	No	No
New York	No	No	Yes	Decoupled	No	No	No
North Carolina	Yes	No	Yes	Decoupled	No	No	Yes
North Dakota	No	No	No	Copies Federal System	No	No	No
Ohio	Yes	Yes (a)	Yes	Decoupled	No	No	No
Oklahoma	No	Yes	Yes	Decoupled	No	No	No
Oregon	No	No	No	Decoupled	No	No	No
Pennsylvania	Yes	No	Yes	Decoupled	Yes	No	No
Rhode Island	No	No	Yes	Decoupled	No	No	No
South Carolina	No	No	Yes	Copies Federal System	No	No	No
South Dakota	No	No	Yes	Copies Federal System	No	No	No
Tennessee	Yes	No	Yes	Copies Federal System	Yes	No	Yes
Texas	Yes	Yes	No	Copies Federal System	No	No	No
Utah	No	No	No	Copies Federal System	No	No	No
Vermont	No	Yes	Yes	Copies Federal System	No	No	No
Virginia	No	Yes	Yes	Copies Federal System	No	No	No
Washington	No	No	Yes	Decoupled	No	No	No
West Virginia	No	Yes	Yes	Copies Federal System	No	No	No
Wisconsin	No	No	Yes	Decoupled	No	No	No
Wyoming	No	No	No	Copies Federal System	No	No	No
District of Columbia	No	No	Yes	Decoupled	No	No	No

(a) Tax phases out completely in 2009. Current score reflects partial phase-out as of July 1, 2008.

(b) No statewide real estate transfer tax, but every county has one.

(c) De minimis tax of 0.01 percent of property value.

**Sources:** Commerce Clearing House, Tax Foundation.

## References

- Agostini, Claudio and Soraphol Tulayasathien (2001). *Tax Effects on Investment Location: Evidence for Foreign Direct Investment in the United States*, Office of Tax Policy Research, University of Michigan Business School.
- Anderson, Patrick (2006). *Benchmarking for Success: A Comparison of State Business Taxes*, Anderson Economic Group, pp. 19-20.
- Bartik, Timothy J. (1991). *Who Benefits from State and Local Economic Development Policies?* Kalamazoo, MI: W.E. Upjohn Institute for Employment Research, 1991.
- Bartik, Timothy J. (1989). "Small Business Start-Ups in the United States: Estimates of the Effects of Characteristics of States," *Southern Economic Journal*, pp. 1004-1018.
- Bartik, Timothy J., (1985). "Business Location Decisions in the United States: Estimates of the Effects of Unionization, Taxes, and Other Characteristics of States," *Journal of Business and Economics Statistics*, Volume 3, No.1, January 1985, pp. 14-22.
- Besley, Timothy J. and Harvey S. Rosen (1998). "Sales Taxes and Prices: An Empirical Analysis," *NBER Working Paper No. w6667*.
- Bittingmayer, Gregory, Liesel Eathington, Arthur Hall and Peter F. Orazem (2005). "Business Climate Indexes: Which Work, Which Don't, and What can They Say About Kansas?" The Center for Applied Economics: Kansas University, June 2005.
- Byars, Jon and Bobby McCormick and Bruce Yandle (1999). *Economic Freedom in America's 50 States: A 1999 Analysis*, Center for Policy and Legal Studies. Clemson University.
- Carroll, Robert and Wasylenko, Michael (1994). "Do State Business Climates Still Matter—Evidence of A Structural Change," *National Tax Journal*, Volume 48, pp.19-38, March 1994.
- Carroll, Robert, Douglas Holtz-Eakin, Mark Rider, and Harvey S. Rosen (2000). "Income Taxes and Entrepreneurs' Use of Labor," *Journal of Labor Economics*. 18, pp. 324-351.
- Chorvat, Terrence R. and Michael S. Knoll (2002). "The Economic and Policy Implications of Repealing the Corporate Alternative Minimum Tax," *Tax Foundation Background Paper*, No. 40.
- Cline, Robert; Neubig, Tom; and Phillips, Andrew (2007). "Total State and Local Business Taxes," Council on State Taxation (COST) with Ernst and Young LLP, April, 2007.
- Due, John F. (1961). "Studies of State-Local Tax Influences on Location of Industry," *National Tax Journal*, Vol. 14, pp. 163-73.
- Fisher, Peter (2005). *Grading Places: What do the Business Climate Rankings Really Tell Us?* Economic Policy Institute, 2005.
- Fleenor, Patrick (1998). "How Excise Tax Differentials Affect Interstate Smuggling and Cross-Border Sales of Cigarettes in the United States," *Tax Foundation Background Paper*, No. 26.
- Fleenor, Patrick and J. Scott Moody (1999). "A Primer on the Economic Implications of Marginal Tax Rates," *Tax Foundation Background Paper*, No. 32.
- Eiras, Ana I., Edwin J. Feulner, Marc A. Miles, Mary Anastasia O'Grady (2004). *The 2004 Index of Economic Freedom*, The Heritage Foundation and The Wall Street Journal.
- Gentry, William M. and R. Glenn Hubbard (2004). "Success Taxes, Entrepreneurial Entry and Innovation," *NBER Working Paper No. w10551*.
- Goolsbee, Austan (2003). "The Impact and Inefficiency of the Corporate Income Tax: Evidence from State Organizational Forms," *NBER Working Paper No. w9141*.
- Goolsbee, Austan and Edward L. Maydew (1999). "Coveting Thy Neighbor's Manufacturing: The Dilemma of State Income Apportionment," revised February, 1999. pp. 3.
- Gupta, Sanjay and Mary Ann Hofmann (2003). "The Effect of State Income Tax Apportionment and Tax Incentives on New Capital Expenditures," *The Journal of the American Taxation Association*, Supplement 2003, pp. 1-25.
- Harden, J. William and Hoyt, William H. (2003). "Do State Choose Their Mix of Taxes to Minimize Employment Losses?" *National Tax Journal*, Volume 56, pp. 7-26, March 2003.
- Haughton, Jonathan and Vadym Slobodyanyuk (2001). *State Competitiveness Report 2001*. Beacon Hill Institute. Boston: Suffolk University.
- Helms, L. Jay, (1985). "The Effect of State and Local Taxes on Economic Growth: A Time Series—Cross Section Approach," *The Review of Economics and Statistics*, Volume 67, Issue 4, November 1985, pp. 574-582.
- Hodge, Scott A. (2003A). "Married Couples File Less Than Half of All Tax Returns, But Pay 74

Percent Of All Income Taxes," Tax Foundation Fiscal Fact.

Hodge, Scott A. (2003B). "Own a Business? You May be Rich: Two-Thirds of Taxpayers Hit by Highest Tax Rate Have Business Income," *Tax Foundation Fiscal Fact*.

Ladd, Helen F. (1998). *Local Government Tax and Land Use Policies in the United States: Understanding the Links*. Northampton, MA: Edward Elgar.

Mark, Stephen T., Therese J. McGuire and Leslie E. Papke (2000). "The Influence of Taxes on Employment and Population Growth: Evidence from the Washington, D.C. Metropolitan Area," *National Tax Journal*, Volume 53, pp. 105-123, March 2000.

McGuire, Therese and Michael Wasylenko (1985). "Jobs and Taxes: The Effects of Business Climate on States' Employment Growth Rates," *National Tax Journal*, Vol. 38, pp. 497-511.

Moody, J. Scott and Wendy P. Warcholik (2004). "How Tax Competition Affects Cross-Border Sales of Beer in the United States," *Tax Foundation Background Paper*, No. 44.

Newman, Robert J. (1983). "Industry Migration and Growth in the South," *Review of Economics and Statistics*, Vol. 65, No. 1, pp. 76-86.

Newman, Robert and Dennis Sullivan (1988). "Econometric Analysis of Business Tax Impacts on Industrial Location: What do we know and how do we know it?" *Journal of Urban Economics*, Vol. 23, pp. 215-34.

Oakland, William H. (1978). "Local Taxes and Intraurban Industrial Location: A Survey," *Metropolitan Financing and Growth Management Policies*, Committee on Taxation, Resources and Economic Development, University of Wisconsin, Madison, pp. 13-30.

Papke, James A. and Leslie E. Papke (1986). "Measuring Differential State-Local Tax Liabilities and Their Implications for Business Investment

Location," *National Tax Journal*, Vol. 39, No. 3, pp. 357-66.

Poletti, Therese (2005). "Incentive-rich Arizona to House New Intel Plant," *San Jose Mercury News*, July 26, 2005. (Online).

Pomp, R. (1987), "Reforming a State Corporate Income Tax," *Albany Law Review*, 3/4, pp. 375-788.

Plaut, Thomas R. and Joseph E. Pluta (1983). "Business Climate, Taxes and Expenditures, and State Industrial Growth in the United States,"

*Southern Economic Journal*, Vol. 50, No. 1, pp. 99-119.

*State Policy Reports*. 1994, Vol. 12, No. 11 (June), Issue 1 of 2, p. 9.

Sullivan, Martin (2003). "The States' Fiscal Mess: How Bad Is It?" *Tax Notes*, Vol. 98, No. 4, pp. 482-486.

Tannenwald, Robert (1996). "State Business Tax Climate: How Should it be Measured and How Important is it?" *New England Economic Review: Federal Reserve Bank of Boston*, Jan/Feb 1996, pp. 23-38.

Tiebout, Charles (1956). "A Pure Theory of Local Public Expenditures," *Journal of Political Economy*, Vol. 64, pp. 416-24.

Vedder, Richard (2001). "Taxes and Economic Growth," *Taxpayers Network, Inc.*

Wasylenko, Michael (1981). "The Location of Firms: The Role of Taxes and Fiscal Incentives," *Urban Affairs Annual Review*, Vol. 20, pp. 155-89.

Wasylenko, Michael (1997). "Taxation and Economic Development: The State of Economic Literature," *New England Economic Review: Federal Reserve Bank of Boston*, March/April 1997, pp. 37-52.



BACKGROUND PAPER  
(ISSN 1527-0408) is  
published approximately  
four times a year. Each study  
explores an economic issue  
in depth, written by  
Foundation economists and  
guest scholars.

Single copy: Free  
Multiple copies: \$ 5 each

The Tax Foundation, a non-  
profit, non-partisan research  
and public education  
organization, has monitored  
tax and fiscal activities at all  
levels of government since  
1937.

© 2008 Tax Foundation

Editor and Communications  
Director, Bill Ahern  
Copy Editor, Alicia Hansen

Tax Foundation  
2001 L Street, NW, Suite 1050  
Washington, DC 20036  
ph. 202.464.6200  
fx. 202.464.6201  
[www.TaxFoundation.org](http://www.TaxFoundation.org)  
[TF@TaxFoundation.org](mailto:TF@TaxFoundation.org)