



ECONOMIC RESEARCH CENTER at THE BUCKEYE INSTITUTE

The Buckeye Institute Policy Brief

How to Grow Ohio's Economy: Return the Budget Surplus to Taxpayers

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Introduction

The Buckeye Institute's *Sustaining Economic Growth: Tax and Budget Principles for Ohio* outlined important principles for keeping Ohio's economy and labor market growing.¹ At the report's release in February 2019, Ohio's projected budget surplus for FY2019 was \$210 million and we analyzed how returning that originally projected surplus to Ohio's families and businesses through permanent tax cuts would affect the state's economy. When Governor Mike DeWine released his budget proposal in March, the Office of Budget and Management revised the estimated budget balance to show that Ohio can now expect a \$658 million surplus for FY2019.²

The governor's budget proposes to spend that surplus on more government services and programs. And the House's recently passed budget provides some tax cuts, but still grows spending faster than current inflation and population growth rates. But increasing government spending will not deliver the same positive, long-term economic results as straightforward tax cuts on personal income and the commercial activity tax. To demonstrate the economic effect of cutting those taxes by \$658 million, we have applied the same dynamic scoring model that we used to analyze fiscal policy proposals in the *Sustaining Economic Growth* report.³ Returning the entire surplus of nearly \$700 million to taxpayers through permanent tax cuts would reduce personal tax liability, create

¹ Rea S. Hederman Jr.; Andrew J. Kidd, Ph.D.; Tyler Shankel; and James Woodward, Ph.D.; *Sustaining Economic Growth: Tax and Budget Principles for Ohio*, The Buckeye Institute, February 21, 2019.

² The estimated surplus is based on the Ohio Office of Budget and Management's estimates for total revenues and expenditures for Fiscal Year 2019 included in FY2020-2021 budget documents.

Budget Recommendations: The State of Ohio Executive Budget Fiscal Years 2020-2021, Ohio Office of Budget and Management, March 15, 2019; and *Budget Highlights: The State of Ohio Budget, Executive Recommendations Fiscal Years 2020-2021*, Ohio Office of Budget and Management, March 15, 2019.

³ We calibrated the model for Ohio using publicly available state and federal data, and relied on a similar dynamic scoring framework used by federal agencies to evaluate federal tax proposals to predict how certain policy changes will affect gross domestic product (GDP), job creation or loss, and government revenue. Our model has undergone a double-blind peer review and incorporated comments from those reviews consistent with current academic standards and methodologies. The model's full technical description provided below will allow researchers to validate the model's accuracy and the conclusions that we have drawn.

Rea S. Hederman Jr.; Andrew J. Kidd, Ph.D.; Tyler Shankel; and James Woodward, Ph.D.; *Sustaining Economic Growth: Tax and Budget Principles for Ohio*, The Buckeye Institute, February 21, 2019.

more than 6,000 new jobs, increase private sector investment, and raise Ohio's gross domestic product by over \$400 million.

Tax Cuts, Not Spending Increases, Will Grow Ohio's Economy

A budget surplus means that Ohio did not need all the tax revenue that it collected. Returning unneeded tax revenues to those who earned it has the decided advantage of promoting sustainable economic growth in ways that more government spending does not. Economic research consistently finds that tax cuts drive more economic growth and job creation than public spending.⁴ In fact, despite attempts to frame government spending as “investing in the future,” economists have demonstrated that government spending not only fails to generate long-term economic growth, but it crowds-out the very sort of private sector investments that *actually* grow economies and create jobs.⁵ Reducing taxes on commercial activity, on the other hand, can significantly increase returns on investment, further encouraging businesses to re-invest in themselves and expand their work forces with more job creation.⁶ Similarly, cutting income taxes for wage earners creates incentives for greater productivity and earning potential by allowing workers to save, invest, or spend their earnings on things that *they*, not the government, deem important.⁷

Rather than continuing to syphon more money than necessary from the private sector, Ohio policymakers should remember the painful economic lessons of the early 2000s and the more recent Great Recession. Tax-and-spend policies that rely on harmful taxes, like the personal income tax and the commercial activity tax, distort market behavior, limit economic growth, and make it more difficult for the state to sustain spending levels during inevitable economic downturns. Instead of promoting new government programs, policymakers should take full advantage of the estimated budget surplus to avoid over-spending, and adopt permanent tax cuts to keep Ohio on the path to prosperity.

⁴ Andrew Mountford and Harald Uhlig, “**What are the effects of fiscal policy shocks?**,” *Journal of Applied Econometrics*, Volume 24, Issue 6 (September/October 2009) p. 960-992; and Karel Mertens and Morten O. Ravn, “**The Dynamic Effects of Personal and Corporate Income Tax Changes in the United States**,” *American Economic Review*, Volume 103, Number 4 (June 2013) p. 1212-1247.

⁵ Valerie A. Ramey, “**Government Spending and Private Activity**,” *Fiscal Policy after the Financial Crisis*, ed. by Alberto Alesina and Francesco Giavazzi (2013) p. 19-55; Kevin B. Grier and Gordon Tullock, “**An empirical analysis of cross-national economic growth, 1951-1980**,” *Journal of Monetary Economics*, Volume 24, Issue 2 (September 1989) p. 259-276; Stefan Fölster and Magnus Henrekson, “**Growth effects of government expenditure and taxation in rich countries**,” *European Economic Review*, Volume 45, Issue 8 (August 2001) p. 1501-1520; and Olivier Blanchard and Roberto Perotti, “**An Empirical Characterization of the Dynamic Effects of Changes in Government Spending and Taxes on Output**,” *The Quarterly Journal of Economics*, Volume 117, Issue 4 (November 2002) p. 1329-1368.

⁶ Abhiroop Mukherjee, Manpreet Singh, and Alminas Zaldokas, “**Do corporate taxes hinder innovation?**,” *Journal of Financial Economics*, Volume 124, Issue 1 (April 2017) p. 195-221; and Xiaobing Shuai and Christine Chmura, “**The Effect of State Corporate Income Tax Rate Cuts on Job Creation**,” *Business Economics*, Volume 48, Issue 3 (July 2013) p. 183-193.

⁷ W. Robert Reed, “**The Robust Relationship Between Taxes and U.S. State Income Growth**,” *National Tax Journal*, Volume 61, Issue 1 (March 2008) p. 57-80.

Economic Effects of Returning the Ohio Budget Surplus to Taxpayers

Sustaining Economic Growth: Tax and Budget Principles for Ohio outlined key principles to help policymakers ensure that Ohio families could keep more of their hard-earned money and encourage continued economic growth through job creation and business investment.⁸ Using the methodology applied in *Sustaining Economic Growth*, we can model the economic effects of reducing the state's personal income tax and commercial activity tax (CAT) by the value of Ohio's projected \$658 million surplus.⁹

The CAT and personal income taxes discourage economic activity and reduce savings and investments year-after-year. Thus, reducing their burdens on families and businesses can spur economic growth even more significantly than one-time tax rebates or increased government spending. Table 1 illustrates the change in tax liability that would be created by lowering the marginal personal income tax rate for all taxpayers. Tax revenues would fall statically by \$414 million. Table 2 demonstrates the change in tax liability that would be realized by reducing the CAT for all levels of businesses. Under changes to the commercial activity tax, revenues would fall statically by \$243 million. Table 3 reveals that returning \$658 million through lower tax rates on businesses and families will generate 6,200 more jobs, increase private investment by \$415 million, and grow Ohio's gross domestic product by \$404 million—all within the first year.

Ohio should return unneeded, surplus tax revenues back to the taxpayers. Growing the state budget will not grow the state economy. Instead, spending today's surplus on tomorrow's government programs risks repeating fiscal mistakes made nearly twenty years ago, and threatens to derail Ohio's still-recovering economy. Permanent tax cuts, however, will expand Ohio's economy, create new jobs, and spur new commercial investment that will make the state even more prosperous than it is today

⁸ Rea S. Hederman Jr.; Andrew J. Kidd, Ph.D.; Tyler Shankel; and James Woodward, Ph.D.; *Sustaining Economic Growth: Tax and Budget Principles for Ohio*, The Buckeye Institute, February 21, 2019.

⁹ Rea S. Hederman Jr.; Andrew J. Kidd, Ph.D.; Tyler Shankel; and James Woodward, Ph.D.; *Sustaining Economic Growth: Tax and Budget Principles for Ohio*, The Buckeye Institute, February 21, 2019; and Andrew J. Kidd, Ph.D., *The Economic Research Center Tax Model Methodology for Ohio*, The Buckeye Institute, February 2019.

Table 1: Personal Income Tax Proposal¹⁰

Ohio Taxable Income	Current Tax Rates	Recommended Tax Rates
<\$10,850	\$0	\$0
\$10,850 - \$16,300	\$80.56 - \$188.47	\$66.46 - \$167.29
\$16,300 - \$21,750	\$188.47 - \$323.41	\$167.29 - \$295.15
\$21,750 - \$43,450	\$323.41 - \$967.68	\$295.15 - \$911.21
\$43,450 - \$86,900	\$967.68 - \$2,473.22	\$911.21 - \$2,360.27
\$86,900 - \$108,700	\$2,473.22 - \$3,336.50	\$2,360.27 - \$3,195.21
\$108,700 - \$217,400	\$3,336.50 - \$8,333.44	\$3,195.21 - \$8,050.84
>\$217,400	\$8,333.44+	\$8,050.84+



¹⁰ These rates are for a single filer but would be proportionately changed for a married couple filing jointly. The exact recommended tax rates for each Ohio Taxable Income group are the following: for incomes between \$10,850 and \$16,300, the rate would be \$66.46 plus 1.850 percent of income in excess over \$10,850; for incomes between \$16,300 and \$21,750, the rate would be \$167.29 plus 2.346 percent of income in excess over \$16,300; for incomes between \$21,750 and \$43,450, the rate would be \$295.15 plus 2.839 percent of income in excess over \$21,750; for incomes between \$43,450 and \$86,900, the rate would be \$911.21 plus 3.335 percent of income in excess over \$43,450; for incomes between \$86,900 and \$108,700, the rate would be \$2,360.27 plus 3.83 percent of income in excess over \$86,900. For incomes between \$108,700 and \$217,400, the rate would be \$3,195.21 plus 4.467 percent of income in excess of \$108,700; and for income above \$217,400, the rate would be \$8,050.84 plus 4.867 percent of income in excess of \$217,400.

Table 2: Commercial Activities Tax Proposal¹¹

Taxable Gross Receipts	Current Tax Rates	Recommended Tax Rates
\$0-\$150,000	\$0	\$0
\$150,000-\$1 million	\$150	\$0
\$1 million-\$2 million	\$800 - \$3,400	\$0 - \$2,250
\$2 million-\$4 million	\$4,700 - \$9,900	\$3,550 - \$8,050
>\$4 million	\$10,400+	\$8,550+



¹¹ The exact recommended tax rates for the commercial activity tax are as follows: for taxable gross receipts less than \$1 million, the rate would be \$0; for taxable gross receipts between \$1 million and \$2 million, the rate would be 0.225 percent of gross receipts in excess of \$1 million; for taxable gross receipts between \$2 million and \$4 million, the rate would be \$1,300 plus 0.225 percent of gross receipts in excess of \$1 million; and for taxable gross receipts above \$4 million, the rate would be \$1,800 plus 0.225 percent of gross receipts in excess of \$1 million.

Table 3: Effect of Lowering Tax Rates with Budget Surplus¹²

	Baseline				
Year	GDP	Employment	Tax Revenue	Consumption	Investment
Year 1	\$621,431	5,507,905	\$26,945	\$442,083	\$127,147
Year 2	\$633,335	5,524,338	\$27,461	\$450,551	\$129,583
Year 3	\$645,467	5,540,819	\$27,988	\$459,182	\$132,065
Year 4	\$657,831	5,557,350	\$28,524	\$467,977	\$134,595
Year 5	\$670,432	5,573,930	\$29,070	\$476,942	\$137,173
Year 6	\$683,274	5,590,560	\$29,627	\$486,078	\$139,800
Year 7	\$696,363	5,607,239	\$30,194	\$495,389	\$142,478
Year 8	\$709,702	5,623,968	\$30,773	\$504,878	\$145,208

	Difference from Baseline				
Year	GDP	Employment	Tax Revenue	Consumption	Investment
Year 1	\$404	6,200	(\$593)	\$109	\$415
Year 2	\$456	6,500	(\$603)	\$112	\$236
Year 3	\$473	6,500	(\$615)	\$116	\$205
Year 4	\$484	6,600	(\$626)	\$119	\$201
Year 5	\$493	6,600	(\$638)	\$122	\$203
Year 6	\$502	6,600	(\$650)	\$125	\$206
Year 7	\$511	6,600	(\$663)	\$129	\$210
Year 8	\$520	6,600	(\$675)	\$132	\$214

¹² Source: The Economic Research Center’s dynamic scoring model. Note: GDP, tax revenues, consumption and investment in millions of 2012 dollars. Employment is full-time equivalent non-farm jobs, rounded to the nearest hundred.

About the Authors



Andrew J. Kidd, Ph.D. is an economist with the Economic Research Center at The Buckeye Institute. In this position, Kidd conducts and produces original economic research that looks at and analyzes the impact of state and federal policies on peoples' lives and on the economy.

Prior to joining The Buckeye Institute, Kidd worked in litigation consulting, providing expert testimony related to economic damages in legal cases. Kidd also served as a research assistant at the UW Population Health Institute at the University of Wisconsin-Madison, which, through its health policy group, performs research and analysis projects on health care access, cost, financing, health system performance, and quality. During his time at the University of Wisconsin-Madison, Kidd's research focus was in demography, education, labor outcomes, and the effects of public policy on labor, education, and health outcomes. He was a College of Letters and Science teaching fellow and was awarded the Anna Morris Ely Teaching Award from the Department of Economics. While there, he taught classes in wages and the labor market, analytical public finance, the principles of microeconomics, and the principles of macroeconomics.

Kidd continues to study questions regarding labor markets and the effects of public policy and demographics on labor market outcomes and behaviors, as well as evaluating health care policy and education policy. A native of Lima, Ohio, Kidd received his bachelor's degree in economics and mathematics from the University of Notre Dame before completing his master's degree and his doctorate in economics from the University of Wisconsin-Madison.



James B. Woodward, Ph.D. is an economic research analyst with the Economic Research Center at The Buckeye Institute. In this position he collects economic data, performs research, and writes about economic policy issues.

Prior to joining The Buckeye Institute, Woodward earned his Master of Public Policy and a Ph.D. in public policy from the University of Kentucky. During his time there, Woodward worked for the commonwealth's Hazard Mitigation Grant program, helping to verify the quality of regional emergency preparedness plans. He also performed policy-related research for the Commonwealth Council on Developmental Disabilities, contributing to a paper on possible, new treatment options for those with disabilities.

Woodward has also spent time researching public economics, health economics, and occupational licensing. His dissertation, *American Obesity: Rooted in Uncertainty, Institutions, and Public Policy*, looked at the role bad public policy (as opposed to consumers and/or market forces) may have played in the rapid increase in obesity rates.

A native of Athens, Ohio, Woodward received his bachelor's degree in economics from Ohio University before going on to complete his graduate studies.



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