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6TH
EDITION

RICH STATES, POOR STATES

ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX



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Rich States, Poor States

ALEC-Laffer State Economic Competitiveness Index

Arthur B. Laffer

Stephen Moore

Jonathan Williams

Rich States, Poor States
ALEC-Laffer State Economic Competitiveness Index
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Table of Contents

About the Authors	iv
Acknowledgements	v
Foreword	vi
Introduction	viii
Executive Summary	ix
Preface: 10 Golden Rules of Effective Taxation	xi
 CHAPTER 1. State of the States	1
Momentum for Pro-Growth Tax Reform Surges	3
The Midwestern Tax Divide	5
Anti-Growth Proposals in the States	5
The Negative Effects of Minimum Wage Laws	9
States Address Huge Unfunded Pension Liabilities	10
Michigan Becomes 24th Right-to-Work State	14
Conclusion	15
 CHAPTER 2. Tax Reform to Fix California's Economy	19
The Current California Tax Structure	21
The Incidence vs. Burden of a Tax	27
Economic Reform: The Principles of Good Tax Policy	30
The Solution: A Flat Tax	32
A Balanced Approach	32
The Results	33
Fixing California	33
 CHAPTER 3. There They Go Again: A New Dose of Junk Economics	37
The Proof Is in the Numbers: Responding to the Critics	41
Population Metrics	42
West Virginia and Nevada: A Case Study in Why Not to Rely Solely On Per-Capita Measures ..	43
Reverse Causation and Population	45
Oil, Sunshine, and Prosperity	45
The 11 States that Adopted an Income Tax	46
Other Economic Factors Our Critics Overlook	48
IRS Data, Moving Van Data, and State Migration	48
Addressing Other Criticisms of Pro-Growth Tax Reform	49
Conclusion	52
 CHAPTER 4. State Rankings: 2013 ALEC-Laffer State Economic Competitiveness Index	55
 Appendix. Economic Outlook Methodology	108
About the American Legislative Exchange Council	110

About the Authors

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Arthur B. Laffer is the founder and chairman of Laffer Associates, an economic research and consulting firm, as well as Laffer Investments, an institutional investment firm. As a result of Laffer's economic insight and influence in starting a worldwide tax-cutting movement during the 1980s, many publications have named him "The Father of Supply-Side Economics." He is a founding member of the Congressional Policy Advisory Board, which assisted in forming legislation for the 105th, 106th, and 107th congresses. Laffer served as a member of President Reagan's Economic Policy Advisory Board for both terms. In March 1999, he was noted by *Time Magazine* as one of the "Century's Greatest Minds" for his invention of the Laffer Curve, which has been called one of "a few of the advances that powered this extraordinary century." He has received many awards for his economic research, including two Graham and Dodd Awards from the Financial Analyst Federation. He graduated from Yale with a bachelor's degree in economics in 1963 and received both his MBA and Ph.D. in economics from Stanford University.

STEPHEN MOORE

Stephen Moore joined *The Wall Street Journal* as a member of the editorial board and senior economics writer on May 31, 2005. He splits his time between Washington, D.C., and New York City, focusing on economic issues including budget, tax, and monetary policy. Moore was previously the founder and president of the Club for Growth, which raises money for political candidates who favor free-market economic policies. Over the years, Moore has served as a senior economist at the Congressional Joint Economic Committee, as a budget expert for The Heritage Foundation, and as a senior economics fellow at the Cato Institute, where he published dozens of studies on federal and state fiscal policy. He was also a consultant to the National Economic Commission in 1987 and research director for President Reagan's Commission on Privatization.

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Jonathan Williams is the director of the Center for State Fiscal Reform and the Tax and Fiscal Policy Task Force at the American Legislative Exchange Council (ALEC), where he works with state policymakers, congressional leaders, and members of the private sector to develop fiscal policy solutions for the states. Prior to joining ALEC, Williams served as staff economist at the nonpartisan Tax Foundation, authoring numerous tax policy studies. Williams's work has appeared in many publications, including *The Wall Street Journal*, *Forbes*, and *Investor's Business Daily*. He has been a contributing author to the Reason Foundation's Annual Privatization Report and has written for the Ash Center for Democratic Governance and Innovation at Harvard's Kennedy School of Government. In addition, Williams was a contributing author of *In Defense of Capitalism* (Northwood University Press). Williams has testified before numerous legislative bodies and spoken to audiences across America. He is a frequent guest on talk radio shows and has appeared on numerous television outlets, including the PBS NewsHour with Jim Lehrer and Fox Business News. Williams was also the recipient of the prestigious Ludwig von Mises Award in Economics.

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Foreword

Even as the nation attempts to recover from the harsh economic conditions of the past several years, no state has embodied the economic potential of America quite like Texas. Our state is a model of prioritizing the core functions of government, limiting its size, and keeping taxes low. These principles, advocated in *Rich States, Poor States*, have helped Texas enjoy a level of economic growth that has led even the *New York Times* to describe Texas as “the future.”

With our population growing by more than 1,000 a day, Texas has gained four congressional seats over the last 10 years. During that same period, the State of New York has lost seats in Congress and, for the first time in history, California failed to gain a single one. From 2001 to 2010, the population of Texas grew by more than 17 percent, compared to just 1.5 percent in New York. Ten years ago, Texas accounted for 7.4 percent of the U.S. economy; today that figure is up to 8.7 percent. Why? It’s simple. Over the last decade, Texas has seen a job growth rate of more than 12.5 percent, far above the national average. Technology giants and small businesses alike are flocking to Texas, many fleeing states with high taxes and burdensome regulations.

In 2013, while many states are still struggling to get their finances in order, Texas has brought in more than we need for essential functions, and maintains a fiscally strong Rainy Day Fund. This fiscal strength is because we hold the line against those who insist we need to raise taxes to boost revenue. Texas is one of nine states that do not levy a personal income tax, and that allows our residents—employers and employees alike—to keep and reinvest more of what they earn. We’re not dependent on any one industry, either. Texas’ economy is fully diversified, thanks in no small part to our efforts to keep government out of the private sector’s way, allowing ample room for greater economic growth.

It is clear that Texas is following a formula for robust economic growth and continued prosperity, a formula based upon the sound principles outlined by Dr. Arthur Laffer, Stephen Moore, and Jonathan Williams in *Rich States, Poor States*. It’s our state’s commitment to these conservative principles that propelled us into, and maintains us in, the national spotlight highlighting our robust and thriving economy.

Unfortunately, we cannot say the same for Washington, D.C. Federal spending is out of control, the federal tax burden is increasing, and federal regulations are being written by activists seeking to restrict and punish industries, rather than help them grow responsibly and create jobs. While the tax and spend

folks in Washington squander away your tax dollars, Texas remains vigilant and committed to preserving the principles of limited government and free markets. The evidence is clear: Economic prosperity is attainable for those states that exercise discretion and discipline in spending and taxation. Pro-growth tax and fiscal policies—like those championed by ALEC and throughout *Rich States, Poor States*—set a clear path to a renewed national economic recovery.

States hold the key to our economic future. States always have, and always will compete for residents, revenues, and industries. Competition is the foundation of success and economic strength in this country. And the stronger our states are individually, the stronger our nation is as a whole. As states continue to sort out budgets and finances, Texas is certainly the example to follow. But no matter which state you're in, by letting people keep more of their money, limiting government interference, and maintaining fiscal discipline, your state can create an environment that fosters opportunity and prosperity for its citizens, while expanding the engine for America's renewed economic growth.

Sincerely,

A handwritten signature in black ink that reads "Rick Perry". The signature is written in a cursive, slightly stylized font. The "R" is large and loops around the "ick". The "Perry" is written in a more fluid, cursive style.

Rick Perry
Governor of Texas

Introduction

I am pleased to see *Rich States, Poor States* in its 6th edition. This edition, like its predecessors, reviews fiscal policies that contribute to economic growth compared to policies that detract from such growth. It has become a go-to source for state policymakers.

States around the country have worked hard to recover from the recent national recession. The measures of economic competitiveness outlined in this report help states gauge how they are faring. And, as the federal government persists in non-growth strategies—taxing, racking up debt, and regulating at disturbing levels—states correspondingly look for ways to improve their own economic performance. In terms of sound fiscal policies, there is no federal role model to follow.

Dr. Arthur Laffer, Stephen Moore, and Jonathan Williams, however, offer important guidance for states. These authors explore fiscal policies that can lead states to “up” their economic game. They provide data and analysis that allow a comparison of practices. They edify in a constructive way, showing the different fiscal policies a state may choose and the effects of those policies on economic growth.

In Wyoming, state executive and legislative officials are ever mindful that a beneficial tax structure, fiscal discipline, and streamlined government contribute to our economic well-being. We want better, not bigger, government. We have a regulatory environment that is reasonable—one that protects our state’s natural beauty but also supports businesses operating in our state and attracts more businesses. We continually work for improvement. We are justifiably proud of our top three industries—energy, tourism, and agriculture—and tout them to no end. We are also trumpeting our state’s natural advantages—abundant electricity, cool climate, ample space, and the like—to develop Wyoming’s reputation as a great place for technology-related businesses.

We have no individual income tax and no corporate income tax. Our state budget is always balanced, and we regularly put money aside into savings. This year, on my recommendation, the Wyoming Legislature reduced ongoing spending by more than 6 percent beginning in July 2013. We want to reverse the trajectory of state budget growth and prepare for unforeseen contingencies. With the support of the Legislature, our executive branch merged two agencies in 2011, consolidated technology services in 2012, and is undertaking a rules reduction project in 2013.

Policies like these inure to the benefit of all our citizens, improving present opportunities and future prospects. Such policies work well in our state—they are not partisan policies, they are simply good policies that yield good results.

I look forward to the thought-provoking discussions that are bound to take place among the many policymakers who will make use of this latest *Rich States, Poor States* report. I thank the American Legislative Exchange Council for continuing to produce it. I thank all those involved in completing it.

Sincerely,



Matthew H. Mead
Governor of Wyoming

Executive Summary

With Congress locked in perpetual gridlock and the U.S. economy stuck in a lackluster recovery, state governments around the country are seeking their own solutions to the country's economic woes. However, the paths that states are pursuing to achieve economic prosperity are not all the same. Some have seen magnificent success in achieving real economic recovery while others continue to struggle.

In this 6th edition of *Rich States, Poor States*, Dr. Arthur B. Laffer, Stephen Moore, and Jonathan Williams highlight the policies throughout the 50 states that have led some states to economic prosperity and others to prolonged real economic recovery. The authors provide the 2013 ALEC-Laffer State Economic Competitiveness Index, based on state economic policies. The empirical evidence and analysis contained in this edition of *Rich States, Poor States* determines which policies lead states to economic prosperity and which policies states should avoid.

In chapter 1, the authors review the most significant state policy developments in a "State of the States" analysis. Laffer, Moore, and Williams provide a new look at the political and economic landscapes of the states after the 2012 election cycle. The authors then outline the highlights and lowlights in the states, from major advances in pension reform to the best and worst changes in state tax policy.

Chapter 2 analyzes California's fiscal woes. This in-depth study of the Golden State's finances is a unique look at the state's economic troubles and provides a starting point for a path to economic recovery. Chapter 2 also serves as a case study for all states regarding what policies not to emulate and how to begin the process of true economic recovery.

In chapter 3, the authors take on some of the most repeated critiques and attacks from big government, pro-tax advocates. Laffer, Moore, and Williams make the concrete case that overall state growth and migration are key drivers of economic prosperity. As citizens "vote with their feet" and move to states that have more opportunities and are more conducive to economic growth, those states will reap the rewards of greater economic prosperity. Critics often take issue with claims that taxes and right-to-work status influence state economies. The authors lay out a point by point case, based on the economic evidence, why taxes and right-to-work status truly matter for economic growth. Overall, this chapter puts to rest some of the most common myths that advocates of higher taxes perpetuate.

Finally, chapter 4 is the highly anticipated ALEC-Laffer State Economic Competitiveness Index comprised of two separate economic rankings. The first ranking is a measure of economic performance based on the three most effective metrics. Growth in gross state product (GSP), absolute domestic migration, and growth in non-farm payroll employment are calculated for each state over ten years. Each of these metrics provides an economic insight into the effects of a state's tax and fiscal policy choices.

The second ranking is of a state's economic outlook moving forward. This forecast is based on a state's current standing in 15 equally weighted policy areas that are influenced directly by state lawmakers. The 15 policy areas have proven over time to be the most influential factors, which state lawmakers can control, in determining a state's economic growth. In general, states that spend less, especially on transfer payments, and states that tax less, particularly on productive activities

such as work or investment, tend to experience higher rates of economic growth than states that tax and spend more.

The following 15 policy variables are measured in the 2013 ALEC-Laffer Economic Competitiveness Index:

- Highest Marginal Personal Income Tax Rate
- Highest Marginal Corporate Income Tax Rate
- Personal Income Tax Progressivity
- Property Tax Burden
- Sales Tax Burden
- Tax Burden from All Remaining Taxes
- Estate/Inheritance Tax (Yes or No)
- Recently Legislated Tax Policy Changes (Over the past two years)

- Debt Service as a Share of Tax Revenue
- Public Employees per 1,000 Residents
- Quality of State Legal System
- Workers' Compensation Costs
- State Minimum Wage
- Right-to-Work State (Yes or No)
- Tax or Expenditure Limits

This 6th edition of *Rich States, Poor States* contains invaluable insight into each of the 50 "laboratories of democracy." With solid empirical research and the latest data on state economies, the evidence is clear on which state tax and fiscal policies directly lead to more opportunities, more jobs, and more prosperity for all Americans.

ALEC-Laffer State Economic Outlook Rankings, 2013

Based upon equal-weighting of each state's rank in 15 policy variables

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

10 Golden Rules of Effective Taxation

1 *When you tax something more you get less of it, and when you tax something less you get more of it.*

Tax policy is all about reward and punishment. Most politicians know instinctively that taxes reduce the activity being taxed—even if they do not care to admit it. Congress and state lawmakers routinely tax things that they consider “bad” to discourage the activity. We reduce, or in some cases entirely eliminate, taxes on behavior that we want to encourage, such as home buying, going to college, giving money to charity, and so on. By lowering the tax rate in some cases to zero, we lower the after-tax cost, in the hopes that this will lead more people to engage in a desirable activity. It is wise to keep taxes on work, savings, and investment as low as possible in order not to deter people from participating in these activities.

2 *Individuals work and produce goods and services to earn money for present or future consumption.*

Workers save, but they do so for the purpose of conserving resources so they or their children can consume in the future. A corollary to this is that people do not work to pay taxes—though some politicians seem to think they do.

3 *Taxes create a wedge between the cost of working and the rewards from working.*

To state this in economic terms, the difference between the price paid by people who demand goods and services for consumption and the

price received by people who provide these goods and services—the suppliers—is called the wedge. Income and other payroll taxes, as well as regulations, restrictions, and government requirements, separate the wages employers pay from the wages employees receive. If a worker pays 15 percent of his income in payroll taxes, 25 percent in federal income taxes, and 5 percent in state income taxes, his \$50,000 wage is reduced to roughly \$27,500 after taxes. The lost \$22,500 of income is the tax wedge, or approximately 45 percent. As large as the wedge seems in this example, it is just part of the total wedge. The wedge also includes excise, sales, and property taxes, plus an assortment of costs, such as the market value of the accountants and lawyers hired to maintain compliance with government regulations. As the wedge grows, the total cost to a firm of employing a person goes up, but the net payment received by the person goes down. Thus, both the quantity of labor demanded and quantity supplied fall to a new, lower equilibrium level, and a lower level of economic activity ensues. This is why all taxes ultimately affect people’s incentive to work and invest, though some taxes clearly have a more detrimental effect than others.

4 *An increase in tax rates will not lead to a dollar-for-dollar increase in tax revenues, and a reduction in tax rates that encourages production will lead to less than a dollar-for-dollar reduction in tax revenues.*

Lower marginal tax rates reduce the tax wedge and lead to an expansion in the production base and improved resource allocation. Thus, while less tax revenue may be collected per unit of tax

base, the tax base itself increases. This expansion of the tax base will, therefore, offset some (and in some cases, all) of the loss in revenues because of the now lower rates.

Tax rate changes also affect the amount of tax avoidance. The higher the marginal tax rate, the greater the incentive to reduce taxable income. Tax avoidance takes many forms, from workers electing to take an improvement in non-taxable fringe benefits in lieu of higher gross wages to investment in tax shelter programs. Business decisions, too, are based increasingly on tax considerations as opposed to market efficiency. For example, the incentive to avoid a 40 percent tax, which takes \$40 of every \$100 earned, is twice as high as the incentive to avoid a 20 percent tax, for which a worker forfeits \$20 of every \$100 earned.

An obvious way to avoid paying a tax is to eliminate market transactions upon which the tax is applied. This can be accomplished through vertical integration: Manufacturers can establish wholesale outlets; retailers can purchase goods directly from manufacturers; companies can acquire suppliers or distributors. The number of steps remains the same, but fewer and fewer steps involve market transactions and thereby avoid the tax. If states refrain from applying their sales taxes on business-to-business transactions, they will avoid the numerous economic distortions caused by tax cascading. Michigan, for example, should not tax the sale of rubber to a tire company, then tax the tire when it is sold to the auto company, then tax the sale of the car from the auto company to the dealer, then tax the dealer's sale of the car to the final purchaser of the car, or the rubber and wheels are taxed multiple times. Additionally, the tax cost becomes embedded in the price of the product and remains hidden from the consumer.

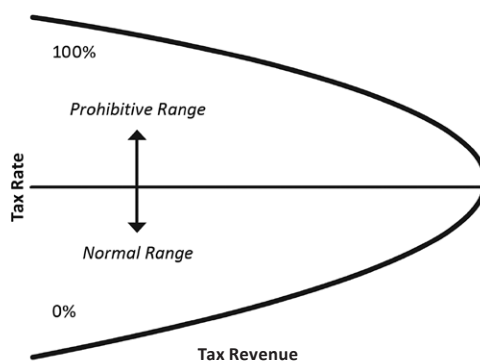
5 *If tax rates become too high, they may lead to a reduction in tax receipts. The relationship between tax rates and tax receipts has been described by the Laffer Curve.*

The Laffer Curve (illustrated to the right) summarizes this phenomenon. We start this curve with the undeniable fact that there are two tax rates that generate no tax revenue: a zero tax rate and a 100 percent tax rate. (Remember Golden Rule

#2: People don't work for the privilege of paying taxes, so if all their earnings are taken in taxes, they do not work, or at least they do not earn income the government knows about. And, thus, the government receives no revenues.)

Now, within what is referred to as the "normal range," an increase in tax rates will lead to an increase in tax revenues. At some point, however, higher tax rates become counterproductive. Above this point, called the "prohibitive range," an increase in tax rates leads to a reduction in tax revenues and vice versa. Over the entire range, with a tax rate reduction, the revenues collected per dollar of tax base falls. This is the arithmetic effect. But the number of units in the tax base expands. Lower tax rates lead to higher levels of personal income, employment, retail sales, investment, and general economic activity. This is the economic, or incentive, effect. Tax avoidance also declines. In the normal range, the arithmetic effect of a tax rate reduction dominates. In the prohibitive range, the economic effect is dominant.

The Laffer Curve



Source: Laffer Associates

Of course, where a state's tax rate lies along the Laffer Curve depends on many factors, including tax rates in neighboring jurisdictions. If a state with a high employment or payroll tax borders a state with large population centers along that border, businesses will have an incentive to shift their operations from inside the jurisdiction of the high tax state to the jurisdiction of the low tax state.

Economists have observed a clear Laffer Curve effect with respect to cigarette taxes. States with high tobacco taxes that are located next to states with low tobacco taxes have very low retail sales of cigarettes relative to the low tax states. Illinois smokers buy many cartons of cigarettes when in Indiana, and the retail sales of cigarettes in the two states show this.

6 *The more mobile the factors being taxed, the larger the response to a change in tax rates. The less mobile the factor, the smaller the change in the tax base for a given change in tax rates.*

Taxes on capital are almost impossible to enforce in the 21st century because capital is instantly transportable. For example, imagine the behavior of an entrepreneur or corporation that builds a factory at a time when profit taxes are low. Once the factory is built, the low rate is raised substantially without warning. The owners of the factory may feel cheated by the tax bait and switch, but they probably do not shut the factory down because it still earns a positive after-tax profit. The factory will remain in operation for a time even though the rate of return, after-tax, has fallen sharply. If the factory were to be shut down, the after-tax return would be zero. After some time has passed, when equipment needs servicing, the lower rate of return will discourage further investment, and the plant will eventually move where tax rates are lower.

A study by the American Enterprise Institute has found that high corporate income taxes at the national level are associated with lower growth in wages. Again, it appears a chain reaction occurs when corporate taxes get too high. Capital moves out of the high tax area, but wages are a function of the ratio of capital to labor, so the reduction in capital decreases the wage rate.

The distinction between initial impact and burden was perhaps best explained by one of our favorite 20th century economists, Nobel winner Friedrich A. Hayek, who makes the point as follows in his classic, *The Constitution of Liberty*:

“The illusion that by some means of progressive taxation the burden can be

shifted substantially onto the shoulders of the wealthy has been the chief reason why taxation has increased as fast as it has done and that, under the influence of this illusion, the masses have come to accept a much heavier load than they would have done otherwise. The only major result of the policy has been the severe limitation of the incomes that could be earned by the most successful and thereby gratification of the envy of the less well off.”

7 *Raising tax rates on one source of revenue may reduce the tax revenue from other sources, while reducing the tax rate on one activity may raise the taxes raised from other activities.*

For example, an increase in the tax rate on corporate profits would be expected to lead to a diminution in the amount of corporate activity, and hence profits, within the taxing district. That alone implies less than a proportionate increase in corporate tax revenues. Such a reduction in corporate activity also implies a reduction in employment and personal income. As a result, personal income tax revenues would fall. This decline, too, could offset the increase in corporate tax revenues. Conversely, a reduction in corporate tax rates may lead to a less than expected loss in revenues and an increase in tax receipts from other sources.

8 *An economically efficient tax system has a sensible, broad base and a low rate.*

Ideally, the tax system of a state, city, or country will distort economic activity only minimally. High tax rates alter economic behavior. Ronald Reagan used to tell the story that he would stop making movies during his acting career once he was in the 90 percent tax bracket because the income he received was so low after taxes were taken away. If the tax base is broad, tax rates can be kept as low and nonconfiscatory as possible. This is one reason we favor a flat tax with minimal deductions and loopholes. It is also why more than 20 nations have now adopted a flat tax.

9 *Income transfer (welfare) payments also create a de facto tax on work and, thus, have a high impact on the vitality of a state's economy.*

Unemployment benefits, welfare payments, and subsidies all represent a redistribution of income. For every transfer recipient, there is an equivalent tax payment or future tax liability. Thus, income effects cancel. In many instances, these payments are given to people only in the absence of work or output. Examples include food stamps (income tests), Social Security benefits (retirement tests), agricultural subsidies, and, of course, unemployment compensation itself. Thus, the wedge on work effort is growing at the same time that subsidies for not working are increasing. Transfer payments represent a tax on production and a subsidy to leisure. Their automatic increase in the event of a fall in market income leads to an even sharper drop in output.

In some high benefit states, such as Hawaii, Massachusetts, and New York, the entire package of welfare payments can pay people the

equivalent of a \$10 per hour job (and let us not forget: Welfare benefits are not taxed, but wages and salaries are). Because these benefits shrink as income levels from work climb, welfare can impose very high marginal tax rates (60 percent or more) on low income Americans. And those disincentives to work have a deleterious effect. We found a high, statistically significant, negative relationship between the level of benefits in a state and the percentage reduction in caseloads.

In sum, high welfare benefits magnify the tax wedge between effort and reward. As such, output is expected to fall as a consequence of making benefits from not working more generous. Thus, an increase in unemployment benefits is expected to lead to a rise in unemployment.

Finally, and most important of all for state legislators to remember:

10 *If A and B are two locations, and if taxes are raised in B and lowered in A, producers and manufacturers will have a greater incentive to move from B to A.*

Salt Lake City, Utah

CHAPTER 1



State of the States

State of the States

Supreme Court Justice Louis Brandeis famously described the states as “laboratories of democracy.” Over the many editions of this publication, we attest to the wisdom of that declaration, as we have witnessed the states rise and fall based on changes in policy. For instance, a decade ago, who would have guessed that Michigan would enjoy real growth in private sector employment and significant gains in economic competitiveness? However, fiscal conservatives in the legislature worked with Gov. Rick Snyder and made significant policy changes, like repealing the hated Michigan Business Tax and enacting a freedom-to-work law, and, by doing so, set the state on the path to renewed competitiveness and economic recovery.

When a state changes policy, for better or worse, it immediately affects the incentive structure for individuals and businesses alike, and the change in incentives directly influences the state’s competitiveness. Through statistical and anecdotal evidence, this publication makes a compelling case that pro-growth fiscal policy is what really makes the difference for economic vitality in the states.

Since the last edition of this publication in early 2012, we have witnessed historic movement toward pro-growth tax reform across the states. Reform minded governors and legislators are working to reform public pensions, prioritize spending, and reshape their tax codes. We are encouraged to see so many policymakers take up the cause of fiscal reform to make their states more competitive. The stakes are incredibly high. According to statistics from the Internal Revenue Service, more than \$2 trillion of wealth has moved across state lines in the past 15 years. What an incredible reward for competitive states. On the

other hand, states with poor policies should be afraid, since capital, both investment and human, is more mobile than ever.

We anticipate the fiscally responsible states will reform government pensions, adopt tax reform and spending restraints, and other pro-growth policies—and they will be rewarded for their actions. On the contrary, the states that value redistribution, punitive tax rates, and bloated government spending will continue to sacrifice economic growth. Additionally, these big government states will increasingly attempt to pick winners and losers in a misguided effort to buy jobs through policies that reek of cronyism. If a state feels like it must offer a special targeted incentive just to attract or retain a company, chances are fairly good that the state’s underlying policy is unattractive for business.

In this chapter, we outline some of the most important policy proposals that have been debated across the 50 laboratories in the past year. As you will read, we have analyzed proposals that will help economic competitiveness as well as those that will harm it. However, by and large, this has been a year where a majority of elected officials have avoided massive tax increases (with the exception of California). Furthermore, competitiveness enhancing tax reform has been on the forefront in many states. While fundamental reform takes time to accomplish, taxpayers across America should be very encouraged as we witness the movement for fiscal reform continue to gain momentum.

The Kansas Uprising

Gov. Sam Brownback campaigned in 2010 promising a tax cut to make the Kansas economy more competitive. But his plan to reduce tax rates and

close loopholes ran into trouble in the Senate, which had been controlled by opponents of tax reform. The governor managed to pass his tax cut, but the Left-leaning Senate coalition refused to cut loopholes and pork spending projects.¹

Rep. Richard Carlson, chairman of the Kansas Committee on Taxation, commented on the tax reform accomplishment, “What a remarkable change one legislative session can make in the course of history when we have a governor with guts and a House with backbone. The legislative session was tense and stressful with all the naysayers in play, but, in the end, the taxpayers of Kansas won the day.”²

Details of the plan:

- Moved from a three tier tax system to two
- Top rate lowered to 4.9 percent from 6.5
- Bottom rate lowered to 3 percent from 3.5
- Non-wage income from pass-through entities exempt from taxation

The most outside of the box section of the plan is the “Small Business Accelerator,” which exempts all non-wage income from taxation for all pass-through entities. This means that the vast majority of small businesses in Kansas are now not subject to an income tax on their business earnings. This includes all sole proprietorships, partnerships, S corporations, and limited liability companies (LLCs).

This bold tax reform was designed to jumpstart small businesses in Kansas and boost economic growth. In the two years of the Brownback administration, with the tax reform less than a year old, results are already starting to show.

- The Kansas unemployment rate has dropped from 7 to 5.5 percent.
- The state has shifted from the second highest income tax rate to the second lowest in the region.
- In 2013, the Kauffman Foundation gave Kansas an A rating for its small business climate; while neighboring Missouri received a C rating.
- In 2012, Kansas had the largest number of new small business filings in state history with more than 15,000.³

After the election of 2012, a new legislative makeup now gives Gov. Brownback a conservative majority and a voter mandate to finish the job of simplifying the Kansas tax code and possibly phasing out the income tax. “This is all about making Kansas a more competitive place to do

business,” Gov. Brownback said.⁴ Voters agreed. Lawmakers are considering plans to provide further tax relief in 2013.⁵

While the Kansas tax reform plan has received criticism from both sides of the political spectrum, the resulting economic growth in Kansas speaks for itself. The plan is not perfect, but it is a bold step toward pro-growth tax reform that will certainly continue to unlock more of Kansas’ economic potential.

Perhaps the greatest compliment for the Kansas tax rate reductions comes from a competitor across the state line. As Missouri Sen. Ed Emery put it, “Kansas has been able to leap ahead. Their new tax policies promote economic freedom and make it hard for Missouri to compete for businesses. When a state is playing catch-up on tax policy, it loses the benefits of leading. The economic benefits align more with the innovator than with those saying ‘me too.’”⁶

Momentum for Pro-Growth Tax Reform Surges

Nebraska, North Carolina, and Louisiana are three states in a growing number that have policymakers considering phasing down or repealing their income tax entirely. Central to the argument in all of these cases is the premise that underlies all six editions of this publication: Taxes matter for competitiveness and economic growth. More to the point, the way taxes are levied matters in addition to the level of taxation. Taxes on income directly harm the incentives for productive activity such as savings, investment, innovation, and hard work. It is encouraging to see so many reform minded governors and legislators tackling fundamental reform.

Nebraska

In Nebraska, Gov. Dave Heineman proposed replacing the income tax with an expanded sales tax that would include services and business-to-business transactions, which are a hidden cost for consumers.⁷ However, the governor had to withdraw his recommendation in the face of opposition from groups currently exempt from the tax, as well as concerns from business and free-market groups that the business-to-business taxes could actually harm growth. A pro-growth sales tax should tax final consumption of goods and

services once, at the retail level. As our friends at the Council on State Taxation recently stated, “Any proposal to extend the sales tax to services primarily consumed by business, without an exemption for business-to-business sales of services required under a retail sales tax, is equivalent to imposing another level of gross receipts taxes on these sales by service providers.”⁸ Tax reformers in other states would be wise to avoid business-to-business taxes altogether.

Louisiana

Louisiana policymakers, in pursuit of higher income and job growth, have floated the elimination of the state’s personal income tax and corporate tax in order to improve their business climate and boost competitiveness. Unlike many other states, Louisiana relies minimally on income and corporate taxes as sources of revenue (14.2 percent and 2.4 percent in 2010, respectively).⁹ Because of this, Louisiana has an easier path to pro-growth tax reform compared to many other states due to the comparatively smaller revenue gap that eliminating the personal income tax and corporate income tax would create.

Before the legislative session, Louisiana Gov. Bobby Jindal had largely led efforts to eliminate the personal and business income tax, primarily through an expansion of the sales tax.¹⁰ But due to some key shortcomings with the governor’s plan (most notably the taxation of business-to-business income, which rightly drew opposition from business groups), the governor has since pulled his tax reform plan and called on the legislature to take the lead on tax reform. Though the governor’s partial withdrawal from crafting the legislation has been viewed by many as a key setback, the prospects for tax reform in the current legislative session live on in Louisiana’s House and Senate.

North Carolina

In North Carolina, a group of state legislators are pushing tax reform that would see the state income tax slashed or eliminated entirely, the corporate and business tax burden significantly reduced, and the estate tax eliminated. North Carolina faces a challenging path to reform given its heavy reliance on personal income tax and corporate income tax (27.9 percent and 4.0 percent,

respectively). However, the widespread support for reform by the state’s fiscally conservative majorities in both houses of the state’s general assembly makes the prospects for at least partial reform in the current legislative session look extremely optimistic.¹¹

Led by State Sen. Bob Rucho, the general assembly has already seen multiple reform bills filed and debated, which attempt to lower and eventually phase out North Carolina’s taxation of personal and business income as well as eliminate the estate tax immediately. Most recently, consensus has been built around a bill that would bring the personal income tax to one flat rate and then gradually lower the rates of the personal income tax and the corporate tax over a period of four years, while gradually broadening the base of the state’s sales tax to include all consumer service transactions. This reform effort would exempt business-to-business sales, a positive sign for both business groups and tax economists who criticize such taxation. The proposal also involves reforms to the state’s franchise tax and elimination of the state estate tax. Given that North Carolina’s business climate has generally lagged behind its regional competitors, this reform would do much to improve the state’s competitiveness and put it on a path to earn the status of one of the nation’s best state tax jurisdictions.

New Mexico Cuts Corporate Tax Rates

While many bold ideas for tax reform have stalled in the 2013 legislative session, New Mexico is a welcome exception. Gov. Susana Martinez came into the session determined to reform the corporate income tax and create more jobs.¹² This was imperative for the State of New Mexico to increase business investment and become a more competitive state in attracting businesses. For many years, New Mexico has had the highest corporate income tax rate in the Southwest region (except for California) at a top rate of 7.9 percent.¹³

The true centerpiece of the reform from this year is the significant cut in the corporate income tax, from 7.9 percent to 5.9, which will make New Mexico more attractive to businesses and will certainly help to grow the state. While there remain some problems with the tax reform package, bipartisan corporate tax rate reduction is certainly a notable success story.

The Texas Margin Tax Proposal

The Texas margin tax is a type of modified gross receipts tax. It is a tax of 1 percent (.5 percent for certain types of businesses) on a business's "taxable margin" as opposed to net profits. It applies to all businesses that have revenues over \$1 million per year and, unlike a normal corporate income tax, it is owed regardless of profits or losses. A business's "taxable margin" is calculated by the least of three options: 1) total revenue multiplied by 70 percent, 2) total revenue minus the cost of wages paid, or 3) total revenue minus the cost of goods sold.

Because of its compliance costs, high revenue volatility, tax pyramiding, and different treatment of businesses based on business models (high margin vs. low margin), there have been efforts in the 2013 session to repeal the tax completely.¹⁴ While these efforts have failed, Gov. Rick Perry has proposed his own tax plan, which would modify the tax. The governor intends to create a \$1 million deduction of the tax for companies with up to \$20 million in revenue; currently, businesses with less than \$1 million in income are exempt from the tax. The governor's plan also includes a provision to allow businesses to deduct moving expenses for relocating to Texas.¹⁵

Gov. Perry's plan would result in a tax cut for Texas businesses of about \$1.6 billion.¹⁶ A full repeal of the tax or any cuts would be pro-growth reforms resulting in Texas unlocking even more economic potential.

The Midwestern Tax Divide

Michigan Passes Phase Out of Damaging Personal Property Tax

Michigan Gov. Rick Snyder, along with a strong majority coalition for reform in both houses of the state's legislature, eliminated the state's personal property tax in 2012. The tax was rightly described by Gov. Snyder as the "second worst tax in the nation," after the Michigan Business Tax (MBT), which was also repealed in 2012.¹⁷ The now eliminated tax forced businesses to pay annual property taxes on their business equipment, infrastructure, and other various business assets.

The tax serves as a massive disincentive to investment and reinvestment of capital into the Michigan economy, and provides a large, unique

expense to doing business in the state of Michigan. Most states have moved away from the taxation of personal property due to the distortionary effect these taxes have on business and their adverse impact on economic growth.¹⁸ The tax will gradually be phased out over the coming decade, providing another economic lift to the State of Michigan, which has seen its business climate radically improve during the past legislative session.¹⁹

Minnesota Governor Targets Taxpayers

One must always take the good with the bad, and not all tax changes moving through the Midwest are growth oriented. Minnesota Gov. Mark Dayton began 2013 calling for a variety of burdensome tax increases: Hiking the gas tax, raising the tobacco and alcohol excise taxes, and initiating the frequently discussed "millionaire's tax" on earners with over \$150,000 in income.²⁰ The proposal was intended to raise \$2.4 billion. By March, however, stiff opposition put the brakes on nearly every proposal, leaving only Gov. Dayton's "snowbird" tax on individuals who live in Minnesota more than two months, but less than six.²¹

Anti-Growth Proposals in the States

Just as there were significant reforms that will help to increase economic growth, many states chose a different path this past year. Higher tax rates in Maryland, New York, Hawaii, Oregon, and California, along with increased regulations, demonstrate a shift away from competitiveness in some states. Costly regulations, such as renewable energy mandates, distort the market and result in increased electricity costs for consumers. These high tax states often implement vast spending programs such as California's \$60 billion highspeed rail boondoggle. We examine some of these anti-growth initiatives below.

California's Massive Income Tax Increase

After the November 2012 election, a huge new tax increase hit California taxpayers. Proposition 30 raised taxes on higher income earners and increased the top individual income tax rate to 13.3 percent.²² This is the rate that many small businesses pay as pass-through entities, and is also now the highest state personal income tax rate

in the nation. In addition to the tax rate increase, Prop. 30 was a retroactive tax increase that applied to income as of January 2012. This retroactivity violates the tax principle of predictability since businesses now owe a new tax bill after they have planned for the year. Unpredictability in the tax code is detrimental for investment and makes it difficult for business planning.

California projects Prop. 30 will raise between \$5.4 and \$7.6 billion between fiscal year 2014 and 2018.²³ However, given the failure of “tax the rich” schemes in other states that we have documented in previous editions of this study, we highly doubt those revenue projections will come to pass. The measure passed with support from teachers unions, since the revenue was promised to go toward educational spending. However, many in California are infuriated that these revenues are now being diverted to the state’s pension fund.²⁴ Read more about California’s broken tax code, its consequences, and possible solutions for the Golden State in chapter 2.

Tax Hikes Redefined in Washington State

Gov. Jay Inslee’s tough stance against higher taxes while on the campaign trail soon disappeared within days of taking office.²⁵ The governor’s proposed budget makes permanent the temporary tax increases that were scheduled to sunset this year. These taxes include an increased beer tax in addition to increased business taxes.²⁶ By making these tax increases permanent, the governor’s plan would impose an additional \$661 million in tax increases on Washington taxpayers over the next three years alone.²⁷

As Erin Shannon from the Washington Policy Center explains, “Under Washington State Law, extending those tax hikes would clearly be considered a tax increase because they are scheduled to expire, and the \$661 million is not part of the projected revenue the state is expected to have when the new biennium starts on July 1.”²⁸ When asked if these tax hikes would violate his campaign promise, Gov. Inslee stated, “We would not be increasing taxes for consumers in that regard.”²⁹ Gov. Inslee chooses to ignore a basic economic principle. It is something about which liberal and conservative economists can agree: Businesses don’t pay taxes, people do. While businesses collect and remit taxes, the economic burden of a tax is always borne by an individual at some level.

If It Moves in Vermont, Tax It

President Ronald Reagan once famously quipped that the Left’s view of the economy could be summarized in three short phases: “If it moves, tax it; if it keeps moving, regulate it; and if it stops moving, subsidize it.” In Vermont, if you drink bottled water, buy snacks from vending machines, or have a sweet tooth, be prepared to pay more this year: The Vermont House of Representatives recently approved a smorgasbord of tax increases.

These taxes include increasing the \$2.62 tax on a pack of cigarettes to \$3.12 and also increasing the \$1.87 per ounce tax on smokeless tobacco and snuff to \$2.60.³⁰ The tax hike package raised the personal income tax for high income earners and capped itemized deductions.³¹ Some of the additional tax hikes include extending a 6 percent sales tax to each item of clothing priced at \$110 or more, increasing the 9 percent meals tax to 9.5 and expanding it to vending machines, while also excluding bottled water, candy, and dietary supplements from the food sales tax exemption.³²

Gov. Peter Shumlin rightly expressed concern over how the tax increases would negatively impact Vermont’s ability to compete with other states for jobs and investments. In an interview with Vermont Public Radio, he remarked, “It’s the wrong thing, wrong time, wrong medicine. And I would argue, totally unnecessary. It’s the tax package that absolutely would be a killer for jobs, and a killer for job growth in the state of Vermont.”³³ Policymakers in Vermont have their work cut out for them, falling one spot and now ranking dead last in our economic outlook rankings of the states this year.

Tobacco Taxes Threaten the New Hampshire Advantage

We often refer to the Granite State’s zero personal income tax, zero sales tax, and low excise tax rates as the “New Hampshire Advantage.” Low, competitive excise tax rates have helped the Granite State to compete for businesses and investments in the economically troubled Northeast. Perhaps one of our favorite and most ironic stories concerns the New Hampshire Advantage and involves a Massachusetts legislator who voted to increase the state sales and alcohol taxes. Soon after his vote, he drove across the state border and purchased liquor at one of New Hampshire’s tax free liquor stores.³⁴ As economist J. Scott Moody ex-

plains, “Whether it’s for cigarettes or chainsaws or big screen TV sets, New Hampshire businesses are winning the competition for shoppers’ dollars.”³⁵

However, a new proposal in the Live Free or Die State may threaten the New Hampshire Advantage. The New Hampshire House passed a budget that would increase the cigarette tax by 30 cents per pack.³⁶ Businesses and state officials in Massachusetts, Vermont, and Maine are the only ones who should welcome this onerous tobacco tax hike. Since New Hampshire has a lower tobacco tax rate than its neighboring states, taxpayers often cross the border to purchase cigarettes at a competitive rate. For example, in a study conducted by Southern New Hampshire University, an estimated 50 percent of all cigarette purchases were derived from out of state smokers.³⁷ Small businesses, such as convenience stores and grocers, would be especially hard hit with a cigarette tax increase.³⁸ Furthermore, the study found that a 5.62 percent increase in New Hampshire’s tobacco tax rate could result in a 6.43 percent decrease in total state revenues.³⁹ As New Hampshire Rep. Laurie Sanborn put it, according to a *New Hampshire Union Leader* article, “When we raise the tobacco tax, we are saying, ‘don’t bother to come to New Hampshire, we don’t need your money.’”

Maryland Drivers Forced to Cough Up More at the Pump

Gov. Martin O’Malley’s radical tax and spend agenda did not let up during Maryland’s 2013 legislative session. The general assembly passed a bill that will increase the state’s gasoline tax by between 13 and 20 cents per gallon while requiring that the gas tax be indexed to inflation, thereby ensuring tax increases well beyond the tenure of Gov. O’Malley.⁴⁰ Tax hikes like these should come as no surprise to Maryland residents. Since Gov. O’Malley took office in 2007, there have been 32 tax, fee, and toll increases (displayed in Table 1 on the following page), estimated to cost taxpayers \$2.3 billion annually.⁴¹ Such increases have contributed to Maryland’s noteworthy drop in its economic outlook rank, moving from 20th in the 5th edition to 35th in this 6th edition.

A 2012 study by the nonpartisan group Change Maryland revealed that the state’s wealthiest residents are being driven out by excessive personal income taxes. The report found that a net 31,000

residents have exited the state since the imposition of a “millionaire’s tax” in 2008. The tax, signed into law by Gov. O’Malley, imposed a personal income tax rate of 6.25 percent on residents with an annual income of \$1 million or more. The study estimates that the out-migration of Maryland residents has had a net negative impact on the state’s fiscal health, costing approximately \$1.7 billion in lost tax revenues over the past five years. The highest levels of out-migration were found in Maryland’s wealthiest counties, suggesting that the state’s higher income residents are the ones “voting with their feet” to avoid excessive taxation.⁴²

Taxachusetts Lives Up to Its Nickname

Policymakers in Massachusetts are considering a vast array of tax increases this year. Taxpayers could see an increase in the gasoline tax, cigarette tax, smokeless tobacco taxes, cigar taxes, and an increased excise tax on utilities, including electric companies.⁴³

Gov. Patrick’s plan would increase the state income tax by 1 percentage point, making the rate for all income earners 6.25 percent. His plan also calls for multi-billion dollar increases in infrastructure and education spending while hiking the gas tax from 21 cents to 51 cents.⁴⁴

Gov. Patrick’s proposal also includes a reduction in the state’s sales tax rate from 6.25 percent to 4.5 percent. Described by some as an attempt to improve the “fairness” of the state’s tax system, the reform still fails to place Massachusetts on competitive footing with nearby New Hampshire, which does not impose taxes on sales or personal income.⁴⁵

Arguing in favor of his sales tax proposal, Gov. Patrick recently stated that the sales tax “is widely regarded to be the most regressive tax that states impose.”⁴⁶ This is an interesting position for the governor to take, considering that he raised the sales tax rate from 5 percent to 6.25 just four years ago. At the time, Gov. Patrick said that the sales tax hike would “bring our budget into balance, offset the need for even more difficult cuts, and expand opportunity throughout the commonwealth.”⁴⁷

When asked for his thoughts on all of these Massachusetts tax increase proposals, New Hampshire Senate Majority Leader Jeb Bradley simply said, “Welcome to New Hampshire!”⁴⁸

TABLE 1 | Maryland Tax and Fee Increases: 2007–2012

Session (tax, fee, toll increase by number)		Increase	Amount (\$ millions)
1. 2012	Special session	New income tax rates at 5% and 5.75% at specified income levels	143.3
2. 2012	Special session	Personal income exemption phase out at specified income levels	35.6
3. 2012	Special session	Recordation tax—indemnity mortgages. Revenue to counties	35.7
4. 2012	Special session	Increases rate for specified tobacco products from 15% to 70%	5
5. 2012	Special session	Death Certificate Fee—\$12 to \$24	0.7
6. 2012	Special session	Repeals sales tax exemption on specified product	0.7
7. 2012		Bay Restoration “Flush Tax”—doubles fee	53
8. 2012		Storm Water Management Fees	341.8
9. 2012		Weights and Measures Registration Fee increase	0.3
10. 2012		Double Lead Poisoning Prevention Fund Fee	2.7
11. 2012		Wetland Water Way Program Fee restructuring	0.3
12. 2011		Hospital assessment	390
13. 2011		Alcoholic beverages—sales tax increase from 6% to 9%	84.8
14. 2011		Vehicle dealer processing change	5.3
15. 2011		Increase in Contractor Licensing and Renewal Fees	0.3
16. 2011		Out of State Attorney Admission Fee	0.05
17. 2011		Vanity Plate Fee—\$25 to \$50	2.5
18. 2011		Birth Certificate Fee—\$12 to \$24	4
19. 2011		Toll increases	90
20. 2010		Fishing License and Registration Fees	3
21. 2009		Speed monitoring system	12.6
22. 2008		Millionaire’s tax—top marginal rate 5.5% to 6.25% ¹	0
23. 2007	Special session	Computer services tax ²	0
24. 2007	Special session	Income tax rates—new marginal rates ranging from 4.75% to 5.5%	163.6
25. 2007	Special session	Sales tax—5% to 6%	613.1
26. 2007	Special session	State corporate income tax—7% to 8.25%	107.9
27. 2007	Special session	Tobacco tax—\$1 to \$2 per pack of cigarettes	121
28. 2007	Special session	Vehicle titling tax—\$23 to \$50	23.5
29. 2007	Special session	Vehicle excise tax increase	39.6
30. 2007	Special session	Electronic gaming tip jar tax	10
31. 2007	Special session	Real property transfer tax	14.1
32. 2007	Special session	Captive Real Estate Investment Trusts	10
Total (32)			2,314

1. Millionaire’s tax in effect through tax years 2008–2010

2. The computer services tax was repealed and replaced with millionaire’s tax

Source: Change Maryland

The Negative Effects of Minimum Wage Laws

The minimum wage has been a controversial topic since its inception in 1938.⁴⁹ Many studies have found that this well-intentioned policy often hurts those that it aims to help. By discouraging employers from hiring inexperienced and unskilled workers, minimum wage laws create a barrier to entry into the labor market, which disproportionately impacts the poor.⁵⁰

To ensure that a hiring decision will have a net positive impact on an organization's bottom line, businesses offer wages that are commensurate with the productivity of the potential employee. If an employee only has the skills to produce \$6.00 per hour worth of value, no rational employer would offer a wage rate of \$9.00 per hour, regardless of the minimum wage rate. Such a decision would clearly represent a loss of value to the employer. Rather than allowing employers to offer a wage rate that is based on the productivity of the employee and enabling unskilled individuals to obtain valuable experience and on the job training, minimum wage laws effectively ban these unskilled individuals from the labor market. Unfortunately, those individuals who have productivity levels below the minimum wage are typically those who need experience and on the job training the most.

Maine Legislature Considers Increasing Minimum Wage

Even with the perverse incentives that go along with minimum wage laws, many states are still considering raising the minimum wage. Most recently, a minimum wage hike was considered this spring in Maine. The Maine House of Representatives has passed a bill that would raise the state's minimum wage to \$9.00 per hour by 2016. The bill would also require that the minimum wage increase annually in proportion to increases in the Consumer Price Index.⁵¹ Advocates of raising the minimum wage say that it has remained at \$7.50 since 2009 and has not kept up with rising prices.⁵²

Gov. Paul LePage has concerns about increasing the minimum wage. "I don't see the point of having the highest minimum wage in the country when our economy is in the tank," he said. Maine is one of 19 states with a minimum wage above

the national level of \$7.25. Of the New England states, only New Hampshire, which has a minimum wage of \$7.25, has a lower minimum wage than Maine. Vermont's minimum wage, \$8.60 an hour, is the highest in the region and is indexed to inflation.⁵³

New York Raises Minimum Wage to New Heights

New York taxpayers are on the hook for the Empire State's new minimum wage policy. New York's state budget will raise the state's minimum wage of \$7.25 to \$9.00 by 2016.⁵⁴ The new policy has sparked significant controversy, especially in the business community. Heather Briccetti, president and CEO of the Business Council of the State of New York said, "Raising the minimum wage would only hurt New York's small businesses, farms, and nonprofits that are struggling to make their current payrolls, and [would] reduce job opportunities in this difficult economy."⁵⁵

In addition to the minimum wage hike, the state will provide a tax credit to businesses that retain or hire 16 to 19-year-old students. The tax credit will reimburse employers for part of the difference in wages as the minimum wage increases.⁵⁶ Sen. Michael Gianaris recognized these perverse incentives and remarked, "We're providing state subsidies that will result in people losing job opportunities and ensuring teenagers are stuck at the minimum wage."⁵⁷ According to the Empire Center, the minimum wage tax credit could cost taxpayers anywhere from \$20 to \$40 million.⁵⁸ So much for economic growth and jobs in the Empire State.

Illinois Driving Out Businesses, Laying Off Working Teens

Gov. Pat Quinn elevated the minimum wage issue to a top priority in Illinois by focusing on it during his 2013 State of the State address. He called for the legislature to increase the wage from \$8.25, already well above the federal mandate, to \$10.00 per hour by 2017.⁵⁹ Legislation before the Senate would link the wage to inflation, which would not take long to make Illinois the highest minimum wage state in America. An editorial in the *Chicago Sun-Times*, by no means a conservative bulwark, pointed out that Illinois could not afford a minimum wage increase, given the ease of moving to neighboring states with lower burdens to entry.⁶⁰

States Address Huge Unfunded Pension Liabilities

Perhaps the most dangerous financial threat to states today is in the area of unfunded pension liabilities for government workers. To be sure, states face tremendously long odds to regain their economic footing in the wake of the downturn. Many states lost more than 20 percent of their entire asset portfolio during the market crash of 2008. A new report by State Budget Solutions estimates the average government employee pension plan is only 41 percent funded. Furthermore, total unfunded liabilities equal nearly \$5 trillion across the 50 states.⁶¹

Unfortunately for pension reform advocates, states have kicked the can down the road for many years, refusing to make tough decisions. In many cases, powerful government employee unions have stopped meaningful reforms in their tracks.

One major challenge in pension policy is the lack of timely and accurate data available to policymakers and the public alike. For far too long our elected officials have relied upon unrealistic pension data, based on faulty assumptions. While greatly outdated even at the time of release, government pension reports have misrepresented the actual financial obligations facing taxpayers.

The lack of pension transparency has been caused, in large measure, by government accounting standards, which have been very “flexible” when compared to standards used by the private sector. For instance, in the case of the major stock market losses of 2008, state and local governments were not required to officially recognize the losses on their books for years. This technique is called asset smoothing, and because it is so widely used, taxpayers and even lawmakers are oftentimes kept in the dark while waiting to learn the full financial impact of a market crash.

Another way the true scope of unfunded liabilities is hidden from taxpayers revolves around assumed rates of return for the investments made by pension funds. Most Americans have suffered some difficult investment losses in their 401(k) plans over the years. When states use an assumed rate of return of eight percent or more to calculate their liabilities, as is the case in a large number of states today, the crisis of pension liabilities is further hidden from public view.

The reform option most discussed by pension reform experts is transitioning away from the traditional, defined-benefit plans into 401(k)-style, defined-contribution plans for new government workers. Private sector employers moved in this direction years ago and many acknowledge the defined-benefit pension model is unaffordable for state taxpayers. A new academic study written by pension reform experts Robert Novy-Marx and Joshua Rauh, reports that, absent reform, the massive unfunded pension liabilities would require huge taxpayer contributions to bail out failing defined-benefit plans. Their report notes, “The average immediate increase is \$1,385 per household per year. In 12 states, the necessary immediate increase is more than \$1,500 per household per year, and in five states it is at least \$2,000 per household per year.”⁶²

The good news, however, is that many states are recognizing fiscal reality and are looking at fundamental pension reform. Michigan, under the leadership of Gov. John Engler in the 1990s, and more recently Utah, serve as models for pension reform. In 1997, Michigan enacted a reform that closed the state’s defined-benefit plan for new employees and set up 401(k)-style personal accounts. A recent actuarial analysis conducted for the Mackinac Center for Public Policy reported that the state has already saved upwards of \$4.3 billion, with the added benefit of workers having portable personal retirement assets.⁶³

One of the greatest problems with defined-benefit plans, outside of the numerous accounting difficulties outlined above, is the perverse incentive structure the plans provide for elected officials. It is astonishingly lucrative for elected officials to have the power to promise lavish future benefits upon government workers, while not having to pay for them up front. Therefore, the 401(k)-style reform may be the key to improving the political incentives for funding pensions, and in the process, solving this major crisis facing state taxpayers. Once again, incentives matter.

Pension Reform Is Not a Partisan Issue

Opponents of pension reform often blame partisan politics as the driving force behind efforts to repair underfunded retirement systems. However, these opponents ignore the bipartisan nature of many successful pension reform efforts around the country. The fact is that pension reform ad-

addresses one of the largest financial problems facing states today, and these efforts have been supported by policymakers from both sides of the aisle.

For example, few would accuse Chicago Mayor Rahm Emanuel, a lifelong liberal and former White House Chief of Staff under President Barack Obama, of being ideologically opposed to pensions or public sector unions. However, Mayor Emanuel addressed the city's \$20 billion pension shortfall in 2012 with a set of concrete recommendations, which included increases in the retirement age and a freeze in cost of living adjustments.

"If we follow along the current path," Mayor Emanuel explained in a letter to city employees, "we know we will confront two stark choices: Either the city's pension payments will squeeze its ability to offer the essential services that you provide, or each of our pension funds will go bankrupt, leaving you and your families without retirement security."⁶⁴ This is hardly an ideological proposition; rather, it is an honest acknowledgment of reality and the consequences of inaction.

Prominent liberals such as former California Speaker Willie Brown and Warren Buffett have also expressed similar concerns about pension underfunding.⁶⁵ In today's political landscape, it's difficult to find an issue that both sides agree on; however, pension reform resonates with individuals from both sides of the aisle. Liberals and conservatives alike have called for pension reform in order to protect taxpayers and ensure retirement security.

There are also several examples of states that have worked across the aisle to reform underfunded pensions. For example, overwhelmingly "blue" Rhode Island enacted major reforms that created a 401(k)-style hybrid plan in 2011. Despite opposition, Rhode Island Speaker Gordon Fox and Treasurer Gina Raimondo (both Democrats) worked together to stabilize the pension system and reduce the state's unfunded liability by \$3 billion.⁶⁶

Utah also directly tackled pension reform in 2011 with the leadership of conservative Senator Dan Liljenquist. Utah eliminated its old defined-benefit pension plan, creating a new system for enrollees hired after July 1, 2011. New employees now have the option of a 401(k)-style plan or a hybrid pension program. Without these reforms,

the Utah retirement fund, which was the nation's best funded before the 2008 crash, would have faced a 50 percent chance of becoming insolvent by 2028.⁶⁷

Successful Pension Reform in Kentucky

One new story of reform comes out of Kentucky, which passed public pension reform legislation in March. The plan, which covers most public employees in the state, excluding teachers, dropped their defined-benefit program with fixed payments in retirement.⁶⁸ The plan was underfunded by nearly \$19.2 billion, jeopardizing the retirement of more than 132,000 state and county employees.

The legislation, which was the result of a 15-month-long task force on the issue, proposed a "hybrid" retirement plan where new employees contribute more of their salaries up front, but are guaranteed a return of at least 4 percent on their investment, more if the state fund performs better than expected. The legislation overwhelmingly passed Kentucky's divided legislature, affirming the argument that pension reform is not a partisan issue.

Illinois Pension Reform Lawsuit

The dire straits of state and local pension funds have become better known recently, but few states find themselves facing financial regulators in federal civil court. This year, Illinois became the second state to settle charges of securities fraud levied by the Securities Exchange Commission for misleading bond investors about the partial payments the state was making to pension funds since 1994.⁶⁹ The state has since hired auditors to improve accounting and oversight of the funds, which allowed the fraud case to be settled out of court, but the \$85 billion funding gap remains unresolved.

Kansas Pension Reform Misfire

Advocates for fundamental pension reform were extremely optimistic this year in Kansas with fiscal conservative legislators capturing a majority in the legislature. A recent study estimated the unfunded liability for Kansas to be \$21 billion.⁷⁰ The need for reform was evident, and the moment seemed perfect to pass an overhaul of the state's pension system that would protect the benefits of current workers and limit the taxpayer's li-

ability for future workers by moving away from a defined-benefit model to a defined-contribution 401(k)-style plan for new hires.

The push for fundamental reform reached its peak in March 2013 when two star experts testified in favor of a 401(k)-style retirement system in a hearing before the House Pensions and Benefits Committee. Bill Bradley, the retired U.S. Senator from New Jersey and a former presidential candidate, and Robert Merton, professor of finance at the Massachusetts Institute of Technology and Nobel laureate in economics, were accompanied to the hearing and other meetings by Kansas Lt. Gov. Jeff Colyer. Bradley and Merton both testified that the current defined-benefit model was unsustainable for state pensions and a 401(k)-style plan was a necessary reform.⁷¹

As the proposal for a 401(k) retirement plan seemed to be gaining ground, a simultaneous measure was introduced to give the Kansas Public Employees Retirement System (KPERs) a quick infusion of cash to meet its obligations by issuing \$1.5 billion in bonds. Both measures were heard in committee for debate, but under intense pressure and skepticism from government unions, the measure for a 401(k)-style pension reform package was tabled. However, the simultaneous proposal authorizing KPERs to sell \$1.5 billion in bond debt did pass the committee and was voted on and passed in the full House of Representatives.⁷²

The result was a double loss for pension reform advocates in Kansas. There would be no structural reform, and the Kansas retirement system and taxpayers would take on \$1.5 billion in additional debt. While the proposal for fundamental pension reform failed this session, fiscally conservative legislators and Gov. Brownback are optimistic that real reform will have a good chance of passing in the future.

Arizona Takes a Stab at Pension Reform

In a bid to start the ball rolling for fundamental pension reform, lawmakers in Arizona are making it personal with a measure to change their own public retirement plan, which covers all elected officials in the state and operates on the common defined-benefit pension model. A 2011 study found that the relatively small fund had an unfunded liability gap of about \$211 million.⁷³ To illustrate the severity of the problem, one esti-

mate claims that the plan supports nearly 1,000 retirees, while only 800 current workers are paying into the system.⁷⁴

The proposed solution is to entirely shut down the current defined-benefit program and replace it with a 401(k)-style defined-contribution plan moving forward. While the plan is still being considered, it is already facing opposition from some members of the legislature. Despite the opposition however, Arizona is poised to become the next state to achieve meaningful and fundamental public pension reform. Speaker Andy Tobin of the Arizona House, and other advocates of the reform effort, hope that by starting with reforming the pension system for elected officials, reforming the other three public retirement systems in the state (which are much larger) could be a smoother process.

Hawaii's Ocean of Red Ink

Unfunded liabilities are putting taxpayers of the Aloha State in a tough fiscal position. In order to make the state's current employee health and retirement systems viable, Gov. Neil Abercrombie admitted that the state would need to spend \$500 million per year for the next 30 years.⁷⁵ Since Hawaii can't afford large yearly payments, the governor proposes spending \$100 million per year instead, meaning that the pension funds wouldn't be financially stable for the next 150 years!⁷⁶

Pennsylvania Gov. Corbett Calls for Pension Reform

According to the Commonwealth Foundation, the Keystone State's pension costs are expected to rise by more than \$2.5 billion over the next four years.⁷⁷ To help address the state's unfunded liabilities, Gov. Tom Corbett called for reforms, including a defined-contribution retirement plan for future state employees. As the governor describes it, "The entire system of state pensions has become a mountain of debt, and the avalanche could bury our economic growth... Resolving our pension crisis will be the single most important thing we do for decades to come."⁷⁸ We couldn't have said it better ourselves.

Unfunded Liabilities Left to Fester: Stockton, CA Files for Bankruptcy

Last year, the city of Stockton became the largest municipality to be the victim of officials not ad-

dressung unfunded pension liabilities. The central California city of roughly 300,000 people became the largest city, so far, to formally file for bankruptcy. While there were many factors that contributed to Stockton declaring bankruptcy, the city's largest creditor was the California Public Employees' Retirement System (CalPERS).⁷⁹

This is likely just the tip of the iceberg, because San Bernardino, CA, (population 213,000) made the same difficult choice by filing for bankruptcy protection last year as well.⁸⁰ The main driver of San Bernardino's budget shortfall is in its personnel costs, which amount to about 75 percent of the city's budget. Furthermore, retirement costs for public pensions are currently taking up 13 percent of the city's budget and are expected to rise to 15 percent or higher in the next three years.⁸¹

We can expect trends like this to continue if state and local governments refuse to address the public pension problems they are facing. In California alone, spending on public pensions rose by 214 percent between 2002 and 2012.⁸² Without fundamental pension reform and a move away from the defined-benefit model, this trend of municipal bankruptcies will most likely continue.

As Stockton continued its bankruptcy proceedings under a federal bankruptcy judge, the city refused to reduce any obligation to their largest creditor, CalPERS, and instead slashed their obligations to municipal bondholders.⁸³

Municipal bondholders lend to cities and municipalities for a multitude of reasons, but most recently (as in this case) to help the municipality finance payments into the public employee retirement system. This has broad negative implications for municipal bonds across the country because there is such a large amount of them, since most municipalities issue some form of bonds for various reasons. In fact, Stockton went even further in cutting its obligations to bondholders by reducing the amount the city owed on the principal of its debt to bondholders. This is the first time that a municipality has been able to do this.

This unfair treatment of debt in Stockton's bankruptcy proceedings has left its municipal bonds nearly worthless. But furthermore, it drastically changes the way that potential municipal bondholders will view investments in the future, and not just for Stockton. Municipal bonds are highly advantageous for investors for two reasons: 1) they are largely regarded as extremely

low risk investments, and 2) they are tax exempt. This has allowed municipalities to attract bondholders to sell debt relatively easily in the past. The problem is that they are clearly no longer as low risk as once thought. This realization led Moody's to downgrade the credit rating of pension obligation bonds for Solano County, CA, and more downgrades are sure to come.⁸⁴

This case is the largest of its kind and will likely set the precedent for municipal bankruptcy proceedings in the future. This is especially true in California, where there are many other large municipalities that are unable to adequately fund their pension obligations, as well such as bankrupt San Bernardino and deeply indebted Los Angeles.⁸⁵

But it's not all bad news for municipalities in California. In fact, at least two major cities in the Golden State have taken the hint and worked to fundamentally reform their pension systems. San Jose passed a pension reform measure by a wide margin last year.⁸⁶ It moved the city in a fiscally responsible direction by increasing employee retirement contributions and mandating that any future benefit increases be brought to the public for a vote. Since these and other changes to public pensions adopted in the initiative address both current workers as well as future hires, the citizens of San Jose face legal challenges from some government unions wishing to overturn the results. So far, the court's decisions have been mixed on the issue. A similar measure also passed last year in San Diego, in which all (non-police) new hires will receive a defined-contribution 401(k) retirement plan like vast majorities of private sector workers.⁸⁷

While it appears likely that many more municipalities will need to file for bankruptcy due to unfunded pension liabilities, citizens are beginning to address the problem responsibly. Unfortunately, as discussed in chapter 2, California's tax and fiscal problems run far deeper than only unfunded pension liabilities and municipal bankruptcies.

Florida Moves to Reduce Unfunded Liabilities

Legislators in the Sunshine State understand the importance of fiscal responsibility. Speaker Will Weatherford has made pension reform a signature issue during his time as House leader. In March 2013, the Florida House of Representatives voted 73-43 in favor of its proposal to require new public

employees, including teachers, police, firefighters, and all state workers, to enter into a 401(k)-style plan. A Senate version would allow new employees to choose between a defined-benefit plan or a 401(k)-style plan. But unless the beneficiary affirmatively opts for a defined-benefit plan, they are automatically enrolled in a 401(k)-style plan.⁸⁸

This is not the first time the legislature has moved to reform Florida's retirement system. In 2011, legislators made several changes, including one that required employees to contribute 3 percent of their salaries to their retirement. Previously, employees were not required to contribute anything.⁸⁹

Florida's total state and local unfunded liability is estimated to be about \$90 billion. A study requested by Speaker Weatherford reported that the state could save \$9.8 billion over 30 years if the bill is passed into law.⁹⁰

Debunking the Transition Cost Argument Against Pension Reform

Despite significant cost savings, those who oppose pension reform often claim that any transition from the current system would result in substantial costs in and of itself. Some claim that even though reforms might produce significant savings, those savings would be outweighed by the costs associated with moving to a new system. A recent study from the Arnold Foundation finds that these claims are incorrect.⁹¹

Common "transition cost" arguments include the claim that creating a new system will deprive existing systems of much needed contributions. However, unlike the Social Security System, state and local pensions are pre-funded, meaning that present day contributions subsidize the future, rather than present day retirees. As the Arnold Foundation study explains, "Moving new workers to a new system does not affect the funded level of past benefit accruals, nor does it affect the debt service payments employers must make to pay off any accrued debt. The pension debt is a bill that is owed to public workers for past service, and this debt must be paid regardless of the go-forward retirement savings system." Therefore, shifting to a new system should not have a substantial effect on the funding levels of existing plans once they are closed. While there may be some rare exceptions in the case of plans that are extremely underfunded, the solution in these cases is compre-

hensive reform, rather than continuation along a path that has shown itself to be unsustainable.⁹²

Other transition cost arguments include the claim that a closed fund must shift toward more conservative investments. These claims are based upon the now debunked theory of "time diversification," which held that risk declines over longer investment horizons. However, because any given year's investment return is independent of the prior year's actual return (as argued by Nobel laureate Paul Samuelson), there is no reason that investment risk should decline over longer horizons. While a closed pension plan will need to move toward more liquid investments in order to make benefit payments in very late stages, there is no need for a closed plan to shift toward more conservative investments. As the Arnold Foundation argues, "The level of risk a government is willing to take with its pension investments should be independent of whether the plan is open or closed."⁹³

Michigan Becomes 24th Right-to-Work State

Michigan, a birthplace of organized labor and still heavily dominated by unions, became the 24th state in the nation to adopt a right-to-work law. Despite widespread union protests in the state capital, Republican Gov. Rick Snyder signed the bill within hours of it passing, calling it "pro-worker and pro-Michigan." The law took effect March 28, 2013, and essentially would prohibit requiring workers to pay union dues as a condition of employment.

Conservatives favor the law because it attracts businesses and provides workers with more choice. It is seen as a much needed counterweight to the excesses of labor unions, particularly in Michigan where the labor agenda has had a deep and lasting impact on the state's public policies. Liberals and union leaders view right-to-work laws as a way to curb the power of labor and reduce its influence.⁹⁴

Later in this edition of *Rich States, Poor States*, the performance of right-to-work states will be discussed extensively, as economic performance of right-to-work states has become the key intellectual grounds for debate on this policy reform. But it's worth noting in advance that both a simple review of the relevant economic performance

data, as well as a review of academic studies that have tried to statistically analyze the effects of right-to-work laws, have found that right-to-work states outperform their compulsory union counterparts, providing their citizens crucial economic opportunity and a pathway to greater prosperity. Michigan was able to drastically improve their business climate and prospects for economic growth with this sound policy reform.

Conclusion

Today, we are witnessing an economic “Balkanization” between states in America. The states with growth as a primary objective will continue to grow if they continue to follow free market policies, while the states with redistribution and regulation as their main objectives will continue to shed jobs and economic vitality if they do not

learn from their mistakes. Our view is that the steady movement of human and investment capital from high tax states to low tax states, which has been present for decades, will continue and likely accelerate over time.

The beauty of the American experiment is this: States are given a great degree of autonomy to choose the best mix of policies for their own citizens. With these 50 states as “laboratories of democracy,” we have the advantage of analyzing what works and what does not. This is not about Republican vs. Democrat—it is about the struggle for capital and job creation that is being fought on an economic battleground. As you will continue to read in this edition of our publication, we believe that not only the theory of our work is sound, but the economic data confirms the case for the limited government model that values economic freedom for all.

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Sacramento, California

CHAPTER

2



Tax Reform to Fix California's Economy

Tax Reform to Fix California's Economy

“Seven years ago, I decided to leave Rancho Santa Fe, CA, for Nashville, TN. That’s a pretty big move for anyone, but particularly for a 65-year-old who had been a southern California resident for 25 years and was dragging his whole family and company along with him,” said Dr. Arthur Laffer.

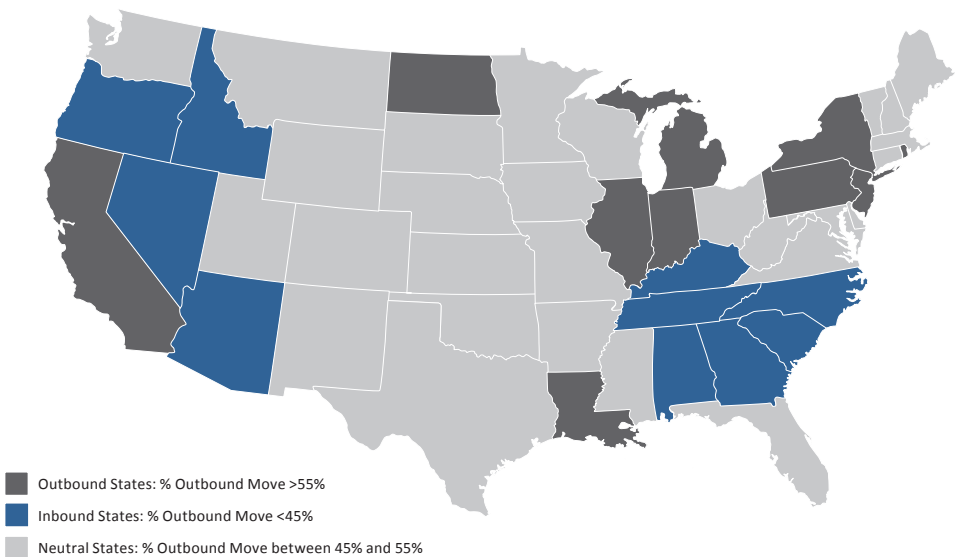
“I can remember the decision to the day. I had been disappointed by the failure of Gov. Arnold Schwarzenegger’s propositions at the ballot box in the fall of 2005, then sat aghast as I read the transcript of his State of the State speech the following January.¹ It became clear to me he would move in a radically different, bigger government direction—a new approach confirmed in his first post-defeat budget.”

Notwithstanding Gov. Schwarzenegger’s proposals, the last thing that California needed was more government spending. The state was already suffocating under a load that included literally hundreds of different government agencies and commissions.

One illustration of California’s desperation when Laffer left the state is contained in Figure 1.²

Yet, as Californians know all too well, this pirouette by the governor was just the icing on the cake. California already had one of the most anti-growth environments in the United States. In fact, companies and people were and are still leaving California in droves.³ The reason is simple: California’s government has imposed upon its citizenry the most onerous business environment in

FIGURE 1 | 2005 Migration Trends Based on United Van Lines Data



Source: United Van Lines 2005 Migration Study

the United States, creating perverse economic incentives in the state. The after-tax rate of return for doing business in California lags so far behind the return in neighboring states (let alone in other no income tax competitors such as Texas, Tennessee, and Florida) that it's no wonder companies, people, investments, and tax revenues are fleeing the state (see Table 2). And yet California raised taxes even further last fall in order to make up for the revenue no longer collected from those businesses that have left the state because of taxes that were already too high.⁴

The intense economic competition between California, the other 49 states, and the rest of the world heightens the need to remedy the economic disincentives created by California's tax and regulatory system. There is no time to waste. California is being hollowed out.⁵

We have consistently highlighted the anti-growth environment in California in the annual publication of this book. In the first four years of the index, California consistently ranked in the bottom 10 states in terms of competitiveness. Last year, California just snuck out of the bottom 10, ranking 38th, largely on the basis of the expiration of a number of temporary tax increases. Well, those temporary tax increases were renewed—and then some. California finds itself ranked 47th in this year's index. California's anti-growth business environment is bringing down

California and the United States as a whole—but not all business can leave the state. Some businesses are not as mobile as others and may not be able to relocate to a different state. These remaining businesses are seriously injured by the political economy in California. It is imperative to turn around the nation's largest state.⁶

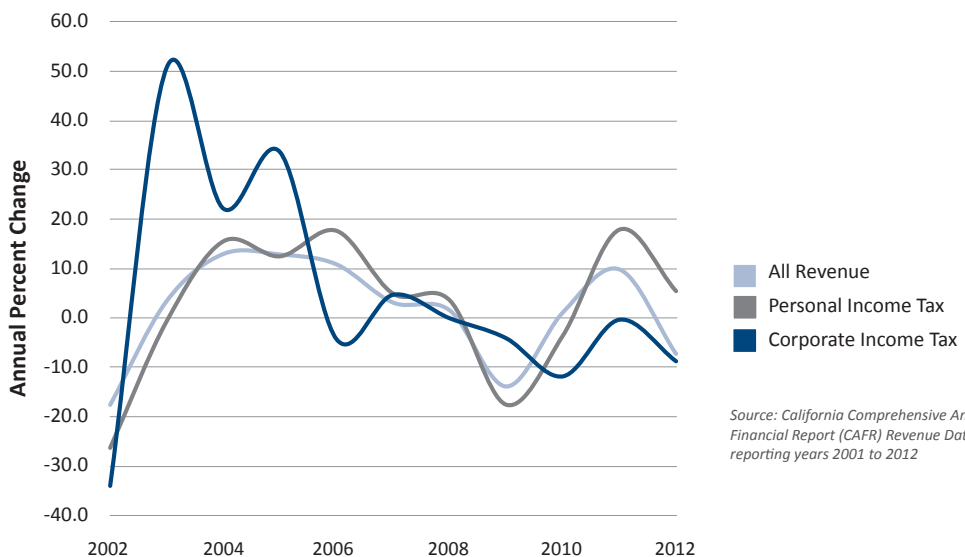
The Current California Tax Structure

Clearly, with such a poor economic policy mix, there are a number of changes necessary to revive the California economy. What becomes clear in analyzing the state is that without drastic policy changes to California's tax and regulatory system, it will remain the Golden State in name only.⁷

Primary among these necessary policy changes is tax reform. At 13.3 percent, California's top marginal personal income tax rate is the highest in the country, and the top marginal corporate income tax rate of 8.84 percent is 22 percent above the national average of 7.2 percent. California's taxes are the most progressive in the nation.⁸

In 2012, personal income tax receipts were 62 percent of California's total revenue, totaling \$53 billion.⁹ In 2011, personal income taxes were 54 percent of revenue.¹⁰ As Figure 2 illustrates, California's tax receipts are highly volatile because they are largely tied to individual and corporate income, which fluctuates greatly from year to

FIGURE 2 | California Revenue Volatility 2001-2012¹¹



year. A look at fiscal year 2009 shows that all revenue—not just income taxes—was down more than 13 percent from the previous year.¹² A state will quickly run into trouble when writing a budget under these uncertain conditions.

But personal and corporate income taxes aren't all that's wrong with the Golden State. California is also a forced union state, which is a serious job killer.¹³ Additionally, California's minimum wage is above the federally mandated minimum wage, the state's tort system ranks 47th in the nation, and California's workers' compensation costs rank 48th in the nation. To make matters worse, a recent study from the American Enterprise Institute estimates California's unfunded pension liability to be just under \$400 billion.¹⁴

Any consideration given to California's regulatory environment paints an even darker picture in both absolute terms and relative to other states. California's energy and housing costs are higher because of both state regulations and the number of activities that are outright prohibited in California.

Despite all of the other necessary changes in California, a number of which are outlined in the recent book *Eureka! How to Fix California*, tax reform is far and away the most important. California's tax codes have been wreaking havoc on the state's finances since they were first introduced in 1936 with a crushing 15 percent highest marginal income tax rate. During good times, revenues have poured in and they've been spent, often on frivolities. Then come the bad times, and revenue shortfalls lead to cuts in essential services, enormously inefficient disruptions in long-term projects, and tax increases that only exacerbate the crises. The first task necessary to bring California back to prosperity is a total overhaul of the state's tax code.

California boasts the single most progressive personal income tax system in the country. Capital gains are taxed as ordinary income.¹⁵ Progressive tax systems magnify tax revenue volatility between periods of boom and bust, and also magnify the boom and bust cycles in terms of both real output and tax revenues. In fact, one of the most significant problems facing California is that high tax revenue volatility inevitably ratchets up government spending in boom times and leads to higher taxes, with the accompanying inevitable decline in prosperity.

Moreover, a highly progressive tax structure means that the most successful and productive of the state's residents and businesses are the ones who are taxed the most (on the margin). The highest income earners are often the ones who make the decision whether to locate a business in California or, if they are already there, whether to stay. The highest income earners are also the primary employers of other people. Their opinions and actions are far more important to the economy than is their share of income. Their political weight, however, still only amounts to one person, one vote.

With this in mind, juxtapose California's high tax rates with the fact that there are nine states in the nation with no state personal income tax at all—including Florida and Texas, and California's neighbors Nevada and Washington. Although there is a high income tax in Oregon, the state lacks a sales tax.¹⁶

Stiff tax competition presents the very serious prospect that California may be hollowed out like Detroit. It is a wonder that California has any entrepreneurs or venture capitalists left.

Income taxes are by far the state's largest source of revenue.¹⁷ In 2009, 0.2 percent of California's income taxpayers (those 33,926 filers with an adjusted gross income of more than \$1 million) paid 24.2 percent of all personal income taxes. The top 3.8 percent (those 555,860 filers with an adjusted gross income over \$200,000) paid 54.5 percent of the state's personal income taxes. California can ill afford to tax the highest income earners to the point at which they choose to leave the state. California's progressive income tax system provides a strong incentive to leave the state for the exceptionally productive residents—those on whom the state is dependent for its revenue base. These wealthy residents, many of whom are baby boomers approaching retirement age, are mobile and could decide to become ex-Californians (see Table 2).

Table 2 provides an overview of the movement of households to and from California, as detailed in the Internal Revenue Service Statistics of Income (SOI) database. These data cover the period 1992 through 2010 and include three important measures: 1) the number of tax returns filed in California by people who filed in California the previous year; 2) the number of tax returns filed in California by people who filed

TABLE 2 | Aggregated California Household Migration Data

	Number of Households	Adjusted Gross Income (AGI) of In-Migrants and Out-Migrants (\$000s)		Average AGI/ Household
18-Year Sum, '92/'93-'09/'10 California Inflows	3,697,622	161,378,278	18-Year Average Annual Household AGI, '92/'93-'09/'10 California Inflows	43,643.80
18-Year Sum, '92/'93-'09/'10 California Outflows	4,580,090	206,774,453	18-Year Average Annual Household AGI, '92/'93-'09/'10 California Outflows	45,146.37
18-Year Sum, '92/'93-'09/'10 Net^^	-882,468	-45,396,175	Average AGI/Household Outflow Premium^	3.44%

Source: Internal Revenue Service, Laffer Associates

^ "AAGI/HHD Outflow Premium" is the income premium of out-migrating households compared to in-migrating households (e.g., a hypothetical 10 percent premium means that the households leaving the state have AGIs that are 10 percent higher on average than households moving into the state).

^^ Net = (inflows to California from that state) - (outflows to that state from California)

in a different state the previous year; and 3) the number of tax returns that were filed in a different state this year by people who filed in California last year.

Not only do we have the number of returns, we also have the aggregate adjusted gross income for each group and the average adjusted gross income over the whole period, per household, for each of these groups. These data allow us to compile the net movements of filers between all other states and California, and the net flows of aggregate adjusted gross income (AGI) between all other states and California for the sum of the years from 1992 through 2010.

It is striking that, over this period, more tax filers—and, with them, their income—chose to leave California for another state than tax filers choosing to leave another state for California. The fact that out-migrants exceed in-migrants represents a huge change from the population magnet that California once was. Given that more income over time has left California, the numbers in Table 2 understate the actual loss of income to California. For instance, a tax filer who left California in, say, 1992 will likely have earned income in 1993 and beyond. Had the tax filer not left California in 1992, he or she would have continued to earn income in California for as long as he or she worked. Thus, all future income for this person will have been lost by California. As a result, by leaving California, the tax filer deprives

the state of his or her income in the year he or she left, as well as in each subsequent year that he or she works but does not reside in California. These numbers are enormous, and constitute a great loss to California.

In the aggregate over this period, California lost more than 880,000 more households than it gained. Another setback for the state is that the households California lost earned more than 3.4 percent more on average than the households it gained. In total, California has lost some \$45 billion in aggregate AGI. Keep in mind that AGI is counted once—only in the first year that the taxpayers leave—but those residents are gone forever. The true AGI lost, counting the income those taxpayers would have earned had they remained California residents, is certainly far larger.

Looking at the destination states for the California taxpayers who left reveals important trends, as well. The data show that Californians are choosing to relocate to those states that more closely adhere to pro-growth economic policies. Table 3 displays the states to which Californians are most and least likely to move based on real world decisions.

The extent to which taxpayers are responding to the incentives described above is represented not only by absolute numbers, but by the average income of California out-migrants, which exceeds the average income of California in-migrants. Moreover, far more people are

leaving California than are entering. It's a double hit on California's bad policies.

California needs a complete tax overhaul—not higher tax rates. Raising taxes, especially during trying economic conditions, will only make matters worse. An economy simply cannot tax itself into prosperity.

In addition, putting a company out of business helps no one, because not only has the company gone under, but the state doesn't get to collect any more tax revenue from that company. The state may even be liable for paying income assistance to the company's former employees and their families. It's a lose/lose situation. Encouraging a person or business to move to another state through higher taxation is squandering opportunity. Yet now, once again, California is levying a larger tax burden on already suffering residents and businesses and could raise tax rates even further on California's most productive citizens.

Excessive taxation is detrimental to everyone—labor and capital, poor and rich, men and women, old and young. In the short run, higher taxes on labor or capital may merely lower after-tax earnings, but in the longer run, mobile factors will “vote with their feet” and leave the state, leaving immobile factors (such as low-wage workers, large fixed capital installations, and land and buildings) to suffer the tax burden.

Although tax rates can be a guide for government instituted disincentives for working, in truth, tax rates are not quite the correct measure of people's incentives to work, produce, and invest. When rates of taxation are low, changes in tax rates are approximately correct as measures of the changes in people's incentives. However, as the level of taxation and regulations increases, changes in tax rates substantially understate their disincentive effects. The higher the level of taxation and regulation, the greater are the disincentive effects of a given tax increase. To see this point clearly, imagine what happens to people's incentives when tax rates rise by 1 percentage point, first from zero and then from 99 percent. The same increase will have very different effects on incentives, depending on what the original rate was.

People do not work to pay taxes; they work to get what they can keep after taxes. It is that

vital incentive that motivates people to give up leisure, switch jobs, learn more skills, or change where they live. Savers do not save to go bankrupt—they save to make an after-tax return on their savings.

Similarly, businesses do not locate their plant facilities as a matter of social concern. They locate their plant facilities to make an after-tax, after all expenses return for their shareholders. It is not necessary for people to focus on all incentives all the time for the overall economy to be driven by incentives incessantly. Rather, economic drivers operate on the margin.

When it comes to motivation considerations for workers, savers, and capital allocators, it is the after-tax return that carries the day, not tax rates specifically. There are some people who will or will not work no matter what the tax rates are. Likewise, there are savers who will save at incredibly low returns and people who will allocate capital inefficiently. There are others who focus their self interest—and, to them, it is the incentive rate that matters.

To demonstrate the difference between tax rates and incentives, let's consider the Kennedy tax cuts of 1963 and 1964. At that time, the highest federal marginal income tax rate was cut from 91 percent to 70 percent while the lowest tax rate (other than zero) was cut from 20 percent to 14 percent. In percentage terms, the highest rate was cut by 23 percent—i.e., a drop of 21 percentage points on a tax base of 91 percent. The lowest rate was cut by 30 percent—i.e., a drop of 6 percentage points from a 20 percent base tax rate.¹⁸

So far, it all seems straightforward. President Kennedy cut the lowest rates in percentage terms by more than he cut the highest rates. But let's look at this from the perspective of two taxpayers—one in the 91 percent marginal tax bracket and one in the 20 percent marginal tax bracket. Prior to the tax cuts, an additional dollar of income for the highest income earner yielded only 9 cents in after-tax incentive. After the tax cuts, an additional dollar of income yielded 30 cents in after-tax income. The highest income bracket tax cut represents an increase in incentives of 233 percent ($21 \div 9$) for a 23 percent cut in tax rates ($21 \div 91$). That is a 10:1 benefit-cost ratio.

Now take the person at the 20 percent

Table 3 | Summary of IRS Migration Data of Most and Least Popular Destinations for California Tax Filers, '92/'93-'09/'10

State	Number of Households	Aggregate AGI (\$000s)	Average AGI/Household				Top CIT Rate (2012)‡	Top PIT Rate (2012)‡	Combined State & Avg. Local Sales Tax Rate (2012)	State & Local Tax Burden as a % of Personal Income (2010)†
			18-Year Average Annual AGI, '92/'93- '09/'10 (Net)^^	18-Year Average Annual AGI, '92/'93- '09/'10 Inflows	18-Year Average Annual AGI, '92/'93- '09/'10 Outflows	AAGI/HHD Outflow Premium^				
Nevada	-184,803	-9,585,640	35,242.09	43,285.03	22.8%	0.00%	0.00%	7.93%	8.2%	
Arizona	-158,600	-7,957,765	37,156.43	42,329.74	13.9%	6.97%	4.54%	9.12%	8.4%	
Oregon	-114,599	-6,075,268	34,287.53	42,382.56	23.6%	11.25%	10.60%	0.00%	10.0%	
Texas	-127,297	-6,023,312	45,398.80	45,969.84	1.3%	2.72%	0.00%	8.14%	7.9%	
Washington	-90,931	-5,332,355	42,735.17	47,201.79	10.5%	8.21%	0.00%	8.80%	9.3%	
Colorado	-65,429	-4,148,274	42,831.61	49,275.93	15.0%	4.63%	4.63%	7.44%	9.1%	
Top 6 States**										
Average of Top 6 States' 18-Year Sums*	-123,609.83	-6,520,435.67	39,608.60	45,074.15	14.52%	5.63%	3.29%	6.90%	8.82%	
California	N/A	N/A	54,313.76	54,313.76	N/A	8.84%	10.30%	8.11%	11.23%	
Average of Bottom 6 States' 18-Year Sums*	25,949.50	1,777,660.00	53,999.57	51,310.41	-4.98%	8.86%	8.03%	7.11%	10.89%	
Bottom 6 States***										
Ohio	14,038	770,752	46,028.99	44,423.61	-3.5%	3.69%	8.43%	6.75%	9.7%	
Michigan	19,256	1,039,901	44,643.34	42,152.82	-5.6%	7.00%	6.85%	6.00%	9.8%	
Massachusetts	27,270	1,409,416	55,591.49	56,803.29	2.2%	8.00%	5.25%	6.25%	10.4%	
New Jersey	25,513	1,929,131	66,899.57	63,597.20	-4.9%	9.00%	9.97%	6.97%	12.4%	
Illinois	29,747	2,353,600	53,400.55	48,009.08	-10.1%	9.50%	5.00%	8.20%	10.2%	
New York	39,873	3,163,160	57,433.46	52,876.46	-7.9%	15.95%	12.70%	8.48%	12.8%	

* equal-weighted averages

** "Top 6 States" are the states that were the most popular destinations for households migrating out of California

*** "Bottom 6 States" are the states that were the least popular destinations for households migrating out of California

^ "AAGI/HHD Outflow Premium" is the income premium of out-migrating households compared to in-migrating households (e.g., a hypothetical 10 percent premium means that the households leaving the state have AGIs that are 10 percent higher on average than households moving into the state).

^^ Net = (inflows to California from that state) - (outflows to that state from California)

† Tax burden is most recent data available

‡ Highest marginal state and local tax rate imposed as of Jan. 1, 2012, using the tax rate of each state's largest city as a proxy for the local tax. The effect of the deductibility of federal taxes from state tax liability is included where acceptable.

Source: Internal Revenue Service, Tax Foundation, Laffer Associates

Table 4 | Economic Incentive After the Effects of Federal, State, and Local Taxes

The percentage of pre-tax income retained by the income earner for a dollar increase in pre-tax income

Personal Income							
State	At \$50,000 Wage Income			State	At \$1,000,000 Wage Income		
	2012	2013	Percentage Change in Incentive from 2012 to 2013		2012	2013	Percentage Change in Incentive from 2012 to 2013
California	56.7%	54.8%	-3.4%	California	45.8%	35.6%	-22.3%
Arizona	61.7%	59.8%	-3.0%	Arizona	52.0%	44.6%	-14.1%
Nevada	64.4%	62.5%	-2.9%	Nevada	55.7%	48.3%	-13.2%
New Mexico	61.5%	59.6%	-3.1%	New Mexico	51.9%	44.5%	-14.3%
Oregon	58.4%	56.5%	-3.3%	Oregon	48.4%	40.8%	-15.7%

Business Income			
State	2012	2013	Percentage Change in Incentive from 2012 to 2013
California	35.2%	28.5%	-19.1%
Arizona	39.7%	34.6%	-12.9%
Nevada	48.1%	42.4%	-11.9%
New Mexico	39.9%	34.8%	-12.7%
Oregon	39.1%	34.1%	-12.9%

Source: Tax Foundation, Laffer Associates

marginal tax rate. For this person, prior to the tax cuts, 80 cents on the additional dollar of income was his after-tax incentive. After the tax cuts, the after-tax incentive was 86 cents on the dollar. That is a 6-cent after-tax increase in incentives on a base of 80 cents, or a 7.5 percent increase in incentives for a 30 percent reduction in tax rates ($6 \div 20$). That represents a 1:4 benefit-cost ratio.

Federal tax rates today aren't nearly as high as they were before President Kennedy cut them, but the effects are similar. Today, we have far more regulations, restrictions, requirements, and mandates from all levels of government than we did before. Back then, there was no earned income tax credit, welfare payments were far lower, and the alternative uses of factors of production were more limited. Everything considered, taxes and regulations today are every bit as

damaging as they were in the mid-1960s.

The following paragraphs will compare California's incentive structure with some of its neighbors in order to show the extent to which California-based factors of production are disadvantaged. A whole host of taxes will be considered. This section will also compare the incentive returns to capital and labor at different levels of income, both at present and hypothetically as though the Bush-era tax cuts had not been passed.

As shown in Table 4 above, in 2012 at earnings of \$50,000 in wages and salary, an additional \$100 of income would net a California resident—after all taxes—\$56.70. This is the incentive effect. Included in this calculation is both the employer and employee federal payroll tax of \$13.30, the federal income tax of \$15, other

state payroll taxes of \$3.00, a state income tax of \$9.30, as well as combined state sales and property taxes of \$6.70. In our 2012 report, these figures did not include the tax increases on both income tax rates and sales tax rates retroactive to Jan. 1, 2012. These tax increases were, however, included in our 2013 calculations. Similar calculations are provided for the neighboring states of Arizona, Nevada, New Mexico, and Oregon, which are representative of all the other states.

We also provide these calculations for people with a wage and salary income of \$1 million and with capital income. Lastly, we provide each of these calculations again for a hypothetical calendar year 2013 in which the Bush-era tax cuts had expired, with the Affordable Care Act's capital taxes, and when California's tax increases are in effect and can be taken into account for planning purposes going forward (rather than being imposed retroactively as they were in 2012, a scenario for which people and businesses are unable to plan).

The first important takeaway from Table 4 is that Californians' take home income over all forms of income is currently much lower than their neighboring states. Second, California's after-tax return for high income wage earners is significantly lower (20 percent) than for low income earners. Third, the drop in the after-tax return for high income earners versus those for low income earners is greater in California than in other states. Fourth, California investors see after-tax returns far below investors in other states. If California continues to raise taxes on high income earners, the gap in take home pay between Californians and their neighbors will continue to rise.

High tax rates are not the only costs that taxpayers must face when they pay their taxes. The economic costs that taxpayers actually incur are far greater than the net sums that the government collects in tax revenues. There are a whole slew of other costs that must be paid, from accountants and lawyers and tax filing firms to recordkeeping and personal filing costs. Beginning with the tax collection process and extending through the benefit disbursement process, a wide array of these compliance costs are associated with the government's vast tax collection infrastructure. These costs can be, and often are, quite large and do just as much damage, dollar for dollar, as the actual taxes paid.¹⁹ The only

difference between these costs and actual taxes is that the government collects nothing from the compliance burden.

The Incidence vs. Burden of a Tax

Taxes are imposed on a wide range of people, organizations, items, or activities. Separate structures exist for taxing corporations, individuals, small businesses, etc. In each case, the tax is paid by the person or structure that it is imposed on. The simplicity of this arrangement, though perfectly logical, sometimes hides the true cost of a certain tax. Just because one person or organization pays the tax to the government, the economic burden of the tax does not necessarily fall on that entity. The difference here is between the incidence of taxation as a payment and the burden of taxation as the cost to be paid.

The incidence and burden of government policies on the various productive sectors of the economy are extremely important features of an economy, such as California's, that has a dysfunctional tax and regulatory environment. When a tax is placed on a particular entity, it does not mean that entity actually bears the burden of the tax. In any tax structure, those factors of production that are either unable or unwilling to vary their work effort in response to price changes will always bear the lion's share of the burden of taxation. In technical terms, the greater the factor's supply elasticity, the smaller will be its burden from a given tax—no matter where that tax is placed. Conversely, the lower a factor's supply elasticity, the greater the factor's burden will be, no matter where the tax incidence is placed. In addition to tax incidence and burden, it is also true that the further away from optimal taxation an economy tax structure is, the greater the damage that will be done by any absolute amount of taxation.

In extreme circumstances, in which the tax on a factor is already within or close to the prohibitive range of the Laffer Curve, any additional increase in that tax, by definition, will elicit large withdrawals of that factor from the productive economy. The end result would be a great deal of damage to the economy and little, if any, additional tax receipts.

When economic theory confronts California's tax structure and regulatory environment,

it is even more disturbing to consider the long-run consequences of these distortions. Capital will, if given enough time, become elastic and leave the state. Out-migration will lead to falling prices for both homes and commercial real estate, which in turn will lead to less housing starts relative to replacement needs. Companies with large capital structures will earn sub-par returns on their investments. Lower returns lead to less new investment and a crumbling infrastructure. Low income workers will lose jobs, and their job skills will also decline. All in all, this is a recipe for an expanding poverty class without the requisite skills to return to the productive labor force. But let's start with a single factor of taxation and then move forward.

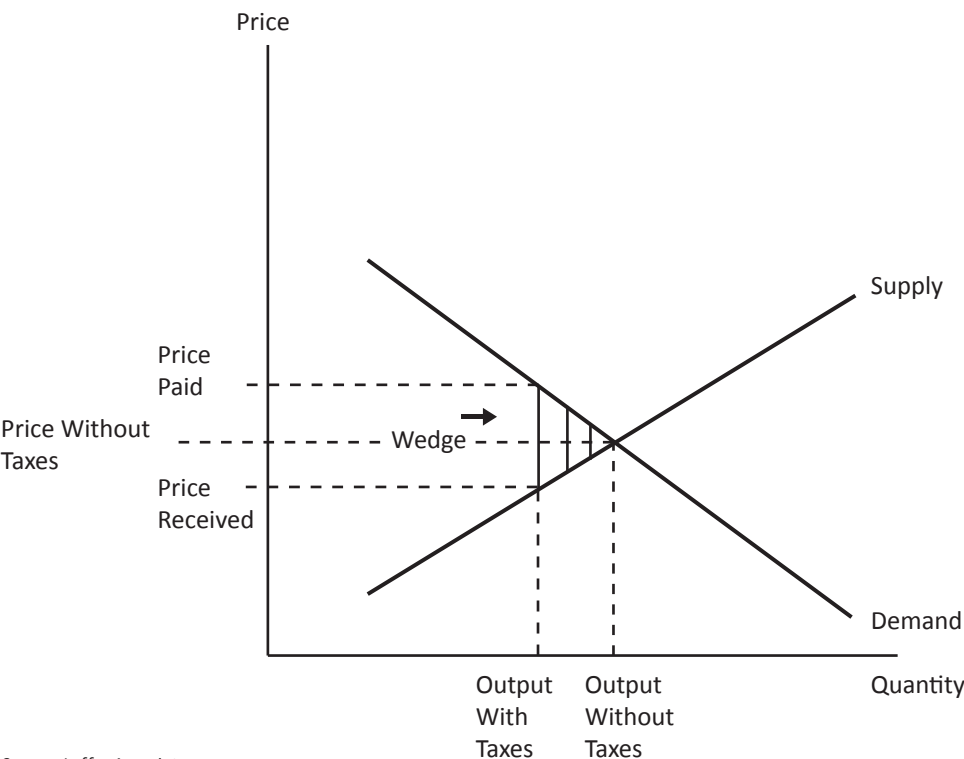
For a single factor with a tax, the difference between what it costs a firm to employ a worker or acquire a unit of capital, and what that worker or owner of capital (saver) receives on net, is measured by the tax wedge (Figure 3). From the standpoint of a single worker or a single unit of capital, an increase in the tax wedge has two

types of effects. First, it raises the cost to the employer in the form of higher wages paid or higher costs paid for each unit of capital used. Or, firms could employ fewer workers and acquire less capital.

On the supply side, an increase in the tax wedge reduces net wages received and the net yields that savers receive. Again, less work effort will be supplied and there will be less saving. In sum, an increase in the tax wedge reduces the demand for, and the supply of, productive factors. An increase in the tax wedge, therefore, is associated with less employment, less investment, and lower output. In dynamic formulations, as the tax wedge grows, output growth falls, and vice versa. Within the context of classical economics, regulations, restrictions, requirements, and explicit taxes are all components of the tax wedge.

However, even after considering the effects of two or more factors, the results derived with only one factor are still applicable. An increase in the tax wedge increases the price paid for and reduces the price received by a factor of production,

Figure 3 | The Tax Wedge



Source: Laffer Associates

reducing both the demand for and supply of that factor. A lower level of economic activity ensues. For example, an increase in the tax wedge on labor will raise wages paid, lower wages received, and reduce the amount of labor employed.

In a two-factor model, though, the process does not stop here. With fewer employed workers, the value of each unit of capital, from the employer's perspective, is lessened. What good is capital if there aren't enough people around to use it? Therefore, the demand for capital falls, less capital will be employed, and the yields paid and the yields received both fall. Taking the process to its final state, an increase in the tax wedge on labor *alone* will lower:²⁰

- output,
- the quantities of both capital and labor employed,
- wages received,
- yields to capital, both paid and received.

In addition, an increase in the tax wedge on labor will raise wages paid.

Similarly, an increase in the tax wedge on the returns to capital will lower:

- output,
- the amount of both capital and labor employed,
- wages received and paid,
- yields received by the owners of capital.

Yields paid for capital will rise.

The incidence of a tax structure is very different from the burden of that tax structure. The person upon whom a tax is levied may well experience no loss in net income if he passes the tax burden forward onto consumers or backward onto suppliers. Likewise, a person upon whom no tax has been levied may suffer large net income losses as a consequence of taxes levied (incidence) on others.

In a two-factor framework, the effects of a tax increase on labor can be radically different depending upon labor and capital's supply elasticity. If, for example, labor supply is very inelastic, an increase in the tax on labor will reduce wages received significantly but barely change wages paid at all. The quantity of labor offered to the marketplace will hardly change, thus leaving

the demand for capital and output unchanged. The cost of capital both paid and received will hardly move and revenues will rise in almost direct proportion to the increase in tax.

Now imagine the supply of labor is highly elastic. An increase in the tax on labor will reduce labor supply if the full cost of the tax can't be passed forward onto capital. If capital is at all elastic, the full cost cannot be passed on to capital. Labor will exit the marketplace in droves, reducing in turn the demand for capital, which too will exit the marketplace. Any increase in tax revenues will come at a dear price in lost output. The more elastic the supplies of labor and capital, the greater the loss in output will be. The higher that existing taxes are prior to the tax increase, the less will be the gain in revenue for any given tax increase—if there is any gain at all. The less elastic the supply of capital, the greater the drop in the price of capital received by savers will be.

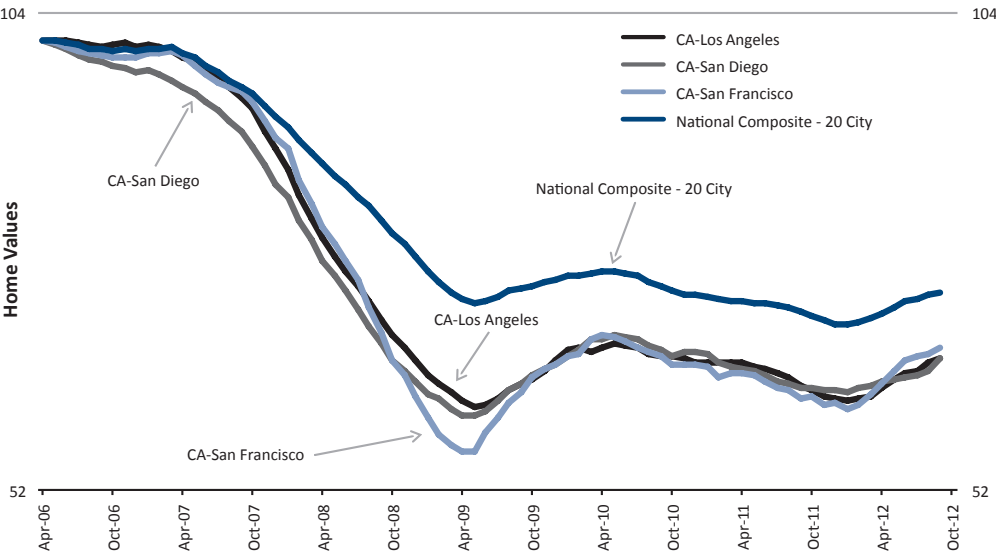
The further away the tax structure is from optimality, the greater is the reduction in overall output for any given tax revenue. As output falls, the net gains to labor from its tax rate cuts will be reduced. The more factors of production that are included in the model, the less that incidence will be related to burden. In the limit, incidence and burden are totally unassociated. In the words of Nobel laureate economist Paul Samuelson:

“Even if the electorate has made up its mind about how the tax burden shall be borne by individuals, the following difficult problems remain:

Who ultimately pays a particular tax? Does its burden stay on the person on whom it is first levied? One cannot assume that the person Congress says a tax is levied on will end up paying that tax. He may be able to shift the tax; shift it ‘forward’ on his customers by raising his price as much as the tax; or shift it ‘backward’ on his suppliers (wage earners, rent, and interest receivers) who end up being able to charge him less than they would have done had there been no tax.

Economists therefore say: We must study the final incidence of the tax total—its effects on commodity prices, factor prices, resource allocations, efforts, and composition of production and consumption. Tax incidence, thus, is no easy

Figure 4 | Case-Shiller California Housing Prices versus National Average Housing Prices
(Monthly, Seasonally Adjusted, April 2006 to September 2012)



Source: S&P Case-Shiller, Laffer Associates

problem and requires all the advanced tools of economics to help toward its solution.²¹

In more intuitive terms, as often as not, taxing capital to spare labor will damage labor. Similarly, taxing the rich is sometimes a good way to further impoverish the poor.

In California today, taxes are universally high across all productive factors when compared to other states. It is also worth noting that taxes in other states are presently very high when compared to their historic norms. With modern markets, communication, and education, factor elasticities have never been higher. California is in serious trouble. It can no longer tax fixed capital with impunity. The fixed capital will leave, as will jobs, output, and tax revenues. If welfare payments per recipient remain as high as they have been, the only group that will not be able to afford leaving is the low wage immobile workers, who soon will drift into the unemployable category.

A clear demonstration of the captive taxpayer effect can be found in housing prices. Houses cannot move when times are bad in a state, so their prices drop instead. In Figure 4 above, the

Case-Shiller San Diego, San Francisco, and Los Angeles housing market price indices are plotted alongside the Case-Shiller national composite price index of 20 cities (also including San Diego, San Francisco, and Los Angeles). The much sharper decline in the three California indices is most likely the consequence of excessive regulatory and tax burdens imposed on fixed factors in California. In the short run, fixed capital cannot leave a state, and, as a captive, it must bear the burden that the state places on it. These data do not bode well for a revival of California's once vibrant home building sector.

Economic Reform: The Principles of Good Tax Policy

In the past, the sole purpose of the tax code has been to raise the necessary funds to run government. Unfortunately, in today's world, taxation incorrectly serves many other goals, including income redistribution, rewarding favored industries, and punishing disfavored behavior. Nowhere is this truer than in California.

Even with these greatly expanded goals for taxation, finding an appropriate tax code would

be relatively straightforward if only people would stop changing their behavior to avoid paying increased taxes.

Positive tax reform can address California's problems in relation to exaggerated economic cycles, long-term growth, and competitiveness vis-à-vis other states. In addition, proper tax reform would greatly mitigate the inevitable boom-bust revenue cycles while also implementing pro-growth economic incentives, leading to stronger growth over time. Comprehensive tax reform can also redress California's uncompetitive tax structure, which would significantly enhance the state's competitive position within the United States and in the global economy.

To find a solution for California's future, we reach back into California's past for the criteria used in judging the efficacy of a state's tax system. These were summarized well in the 19th century by Californian Henry George.²²

The best tax by which public revenues can be raised is evidently that which will closest conform to the following conditions:

1. That it bears as lightly as possible upon production—so as least to check the increase of the general fund from which taxes must be paid and the community maintained.
2. That it be easily and cheaply collected, and fall as directly as may be upon the ultimate payers—so as to take from the people as little as possible in addition to what it yields the government.
3. That it be certain—so as to give the least opportunity for tyranny or corruption on the part of officials, and the least temptation to law-breaking and evasion on the part of the taxpayers.
4. That it bear equally—so as to give no citizen an advantage or put any at a disadvantage, as compared with others.

California's current tax codes grossly violate each one of Henry George's conditions for the "best tax."

California's current tax code also violates our more modern take on George's maxims. We now have an extra century of experience with taxation, but the lessons have not changed much.

The Keys to Good Tax Policy

Simplicity: The tax code should be easy for the average citizen to understand, and it should minimize the cost of complying with the tax laws. Tax complexity adds cost to the taxpayer, but does not increase public revenue. For governments, the tax system should be easy to administer, and should help promote efficient, low cost administration.

Transparency: Tax systems should be accountable to citizens. Taxes and tax policy should be visible and not hidden from taxpayers. Changes in tax policy should be highly publicized and open to public debate.

Economic Neutrality: The purpose of the tax system is to raise needed revenue for core functions of government, not to control the lives of citizens or micromanage the economy. The tax system should exert minimal impact on the spending and decisions of individuals and businesses. An effective tax system should be broad-based, utilize a low overall tax rate with few loopholes, and avoid multiple layers of taxation through tax pyramiding.

Equity and Fairness: The government should not use the tax system to pick winners and losers in society, or unfairly shift the tax burden onto one class of citizens. The tax system should not be used to punish success or to "soak the rich," to engage in discriminatory or multiple taxation, or to bestow special favors on any particular group of taxpayers.

Complementary: The tax code should help maintain a healthy relationship between state and local governments. The state should always be mindful of how its tax decisions affect local governments so they are not working against each other—with the taxpayer caught in the middle.

Competitiveness: A low tax burden can be a tool for a state's private sector economic development by retaining and attracting productive business activity. A high quality revenue system will be responsive to competition from other states. Effective competitiveness is best achieved through economically neutral tax policies.

Reliability: A high quality tax system should be stable, providing certainty in taxation and in revenue flows. It should provide certainty of financial planning for individuals and businesses.

Source: ALEC's Tax and Fiscal Policy Task Force. Statement of Tax Principles.

Taking into account both the lessons from Henry George and more recent insights into taxation, the best form of taxation is a broad-based, low rate flat tax. Taxes are a negative incentive, like scolding. You know exactly what people will try not to do: They will try not to report taxable income. However, it is unclear how they will act on their aversion to reporting that taxable income. They will use evasion, avoidance, and the underground economy; they will use tax loopholes; they might even go out of business and become unemployed; or they might get up and move to a neighboring state. They will do all they can to avoid reporting taxable income. People don't like taxes. The whole theory behind a low rate flat tax, very simply, is that the best tax has the lowest possible tax rate on the broadest possible tax base that is economically sensible. The best tax provides people with the least incentives to evade, avoid, and otherwise not report taxable income, and symmetrically provides people with the fewest places to which they can escape to avoid the tax.

The Solution: A Flat Tax

Our central proposal to restore prosperity to California, and to other states, is for California to adopt a broad-based, low rate flat tax. The low rate and broad base provides the least incentive to evade, avoid, or otherwise not report taxable income.

This tax code would be incredibly simple. Unlike the current tax code, compliance would cost very little in addition to the taxes paid. Companies in California currently spend huge amounts of money complying with the tax code, resources that could be put to better use in other areas.²³ Instead, taxes will be easier to understand, making the system much more efficient, saving time and money for companies big, small, and everywhere in between.

A Balanced Approach

The progressivity of an income tax like California's causes revenue surges during strong economic periods that are disproportionate to the growth in income. During recessions, progressive tax systems cause revenues to crash further than the accompanying income decline. The transitions between economic booms and busts introduce biases because the growth pattern of tax revenues will not change with the same timing as the growth pattern of economic activity. For instance, the peak in the tax revenue surge that resulted from capital gains and stock options occurred in FY 2001—the calendar year when all three major stock indices tanked. The asynchronous timing of tax revenue declines compared to declines in the economy partially explains why tax revenues were peaking while the economy was declining.

A flat rate tax achieves a stable, steady source of revenues for both state and local governments. Stability allows the government to plan more effectively and avoid cutting critical programs in one year and expand them the next, which is exactly what is currently happening. A flat tax would also avoid the yo-yo effect seen from ad hoc taxes and deductions.

We believe that this reform should be set into a state's constitution, so that there is a single tax rate and taxpayers and politicians can know exactly how to plan for every year. The state and local governments should each receive a fixed percentage of total revenues, adding to 100 percent.

Astute Californians will recognize that this proposal is very similar to the federal proposal made by current Gov. Jerry Brown, when he ran for president in 1992. In fact, Gov. Brown and Dr. Laffer developed that proposal together. The

low rate flat tax that he proposed for the United States had a tax rate of 13 percent. It was a flat tax rate for one and for all. This flat tax system addresses the problems that California has today, of highly volatile revenues, extreme disincentives to long-term growth, and adverse barriers to California's competitive position.

Our research indicates that across all states and over time, high taxes inhibit state economic growth and population growth.²⁴ The converse is also true: Low tax states experience higher growth rates in production and population. The surge in economic activity that would result in California after shifting to a broad-based, low rate flat tax would be astounding. The after-tax rate of return for doing business in California would rise, both because of the decrease in tax rates and the elimination of a myriad of fees that only serve to decrease productivity. The result would be more businesses moving into California, fewer existing California businesses leaving, and more economic activity brought out from the underground economy.²⁵ The California economy would soar and the budget deficit would shrink.

Again, by having the largest possible tax base combined with the lowest possible tax rate, people are provided the least opportunity to avoid paying taxes and the lowest incentive to do so.

Reducing the incentives to avoid or evade taxes results in a reduction in the associated costs of monitoring these activities. In addition, lower tax rates go hand in hand with greater incentives to work and produce.

Under a flat tax structure, productive Americans will find it more profitable to save, invest, and produce in their state, and less profitable to employ accountants and tax specialists or find other ways to avoid paying taxes. The net result is faster economic growth, more jobs, a much larger economic pie, increased tax revenues, and increased prosperity for all Californians.

The Results

Pro-growth tax reform will benefit the poor, minorities, and the disadvantaged enormously because it will create jobs, output, growth, and appreciation of asset values. Workers' pension funds will rise sharply, keeping pace with rising asset values.

The flat tax is designed to minimize the disincentives induced by tax rates and yet still provide the requisite amount of revenues to provide the necessary services, even at the state and local level. This static revenue neutral proposal will, by definition, raise the same amount of revenue as the current system, if all incomes stayed the same. But, in truth, every state stands to gain from its implementation. The broad-based, low rate tax minimizes distortions and maximizes efficiency gains. The state's competitive environment would increase and economic activity and in-state asset values would increase. Tax revenues would soon exceed the most optimistic projections. The longer this new tax system is in place, the greater these gains will be.

The key to good tax reform is to look not only at how budget problems can be solved this week, this month, or this year, but to set into place a system that will not cause state and local governments to have the same crisis every decade. An ounce of prevention is worth a pound of cure. Our current crisis is exactly the same crisis we had from 1992 to 1995, and again from 2001 to 2003. The only solution to the revenue crisis is to eliminate the unsustainable revenue surges. The low rate flat tax would have provided local governments with stable, steady revenue, minimizing the risk of schoolteachers or police officers being fired.

Fixing California

Even after moving to a flat tax, California would still, without question, have a number of remaining policies that negatively affect its competitiveness vis-à-vis other states, but the improvements the flat tax would bring in the incentives to work, save, produce, and invest for California businesses and citizens would be tremendous, as would the benefits to the California state budget. This one reform is the major change that would set California back on the path to prosperity. This single dramatic change in policy would cause a rapid change in the state's trajectory, allowing it to replenish its capital stock and begin attracting people and business once again.

California's fiscal crisis, to a great extent, is the consequence of its ad hoc accumulation of taxes, fees, and regulations. California is in perpetual budget crisis mode because of the boom

and bust cycle and tax rates that continually drive productive citizens elsewhere. The state faces an astounding \$617 billion in debt and unfunded pension obligations—and that’s just for the state, not even taking into account local governments. The late *New York Times* columnist Bill Safire used to refer to these numbers as “MEGO” numbers, an acronym for “My Eyes Glaze Over.”²⁶ California chose to balance its budget by raising existing taxes. With California’s unemployment rate at 9.4 percent, it makes no sense to raise taxes on the dwindling number of people who are working.²⁷ For those who are currently working and avoiding taxes, they will never start to pay taxes under the current tax system. Higher tax rates will not make anyone’s life better, and the government will not collect more revenue. It makes no sense to raise taxes on a business that is already in trouble. A business that is having a hard time making it now will be pushed under with higher taxes. It is these businesses that create employment.

People and businesses vote with their feet—it is common sense. We found this to be true in California in the early to mid-1990s, when taxes were raised dramatically in the state. Go back and look at Figure 1 carefully to see how the same pattern occurred in 2005. California became an economic supernova, radiating individuals, jobs, and businesses to neighboring states. Raising taxes did not work then and will not work now. The promised revenues never came.

If California could collect more revenue from

a tax increase, those taxes would come from the very people that the state governs. It is unlikely that Sacramento knows better how to spend those dollars than the people who earned them. It makes no sense to make California’s citizens go bankrupt in order to make the state’s government solvent. Economics is double-entry bookkeeping. For every dollar the state collects, there is someone who loses that dollar and who also has a budget to balance. In this situation, you either lose people (they lose their jobs or they leave the state) or you put the private sector fiscal system out of order by trying to put the state’s fiscal situation in order. Growth is the only answer that works for both.

By setting anti-growth incentives everywhere, California’s tax code costs a lot more than just the taxes that the government collects. This counterproductive tax code has been the result of both Republican and Democrat policies—it’s not a political or partisan system.

The lessons learned from our analysis of the states is that a low rate flat tax calculated to be statically revenue neutral will, paradoxically and in short order, result in more tax revenue. That revenue will be raised at far lower cost to both taxpayers and state government.

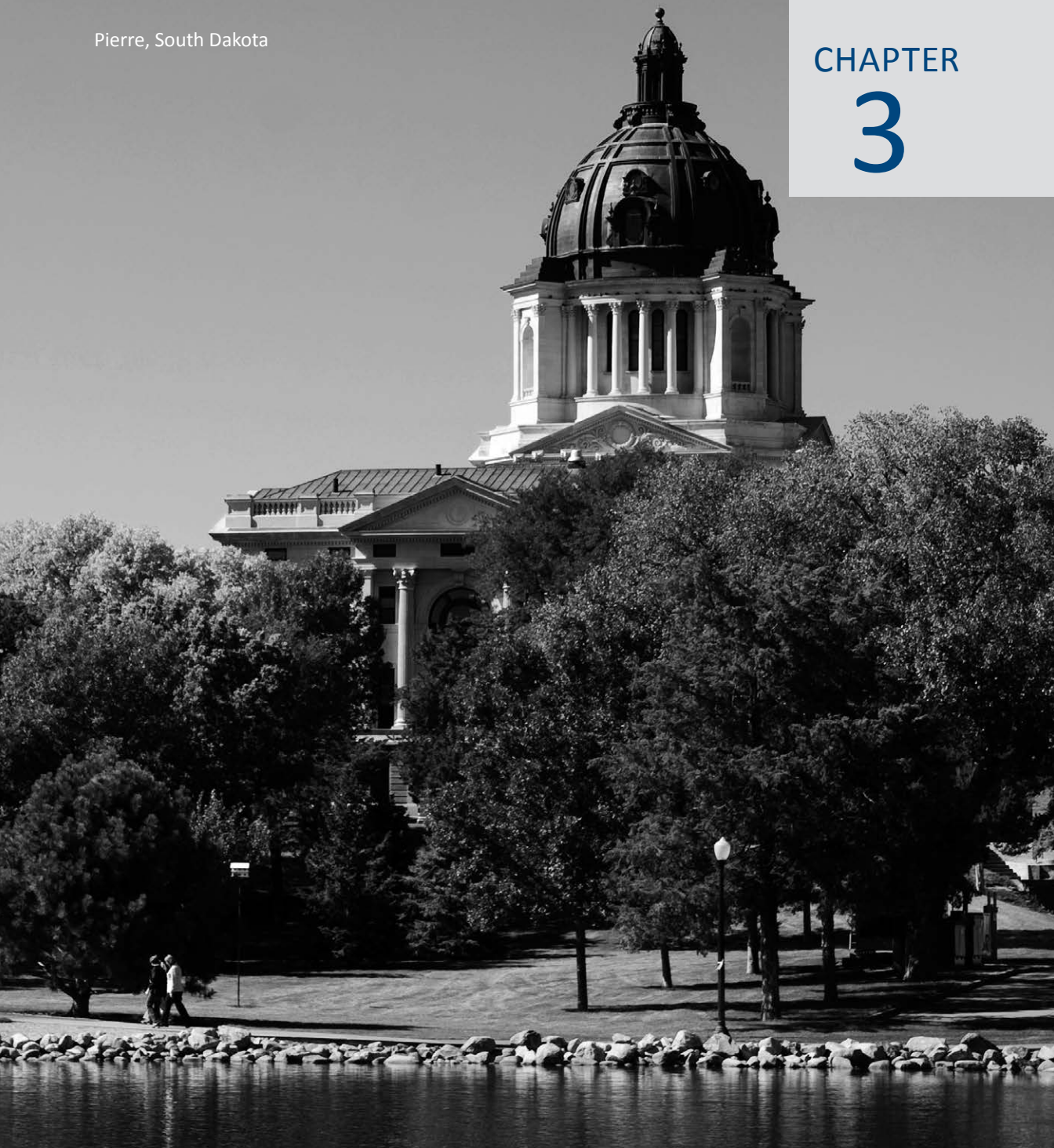
If California were to institute a low rate flat tax, the after-tax rate of return on businesses would increase dramatically, economic incentives for growth would improve, and people and businesses would once again find the business prospects available in California to be golden.

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Pierre, South Dakota

CHAPTER
3



There They Go Again: A New Dose of Junk Economics

There They Go Again: A New Dose of Junk Economics

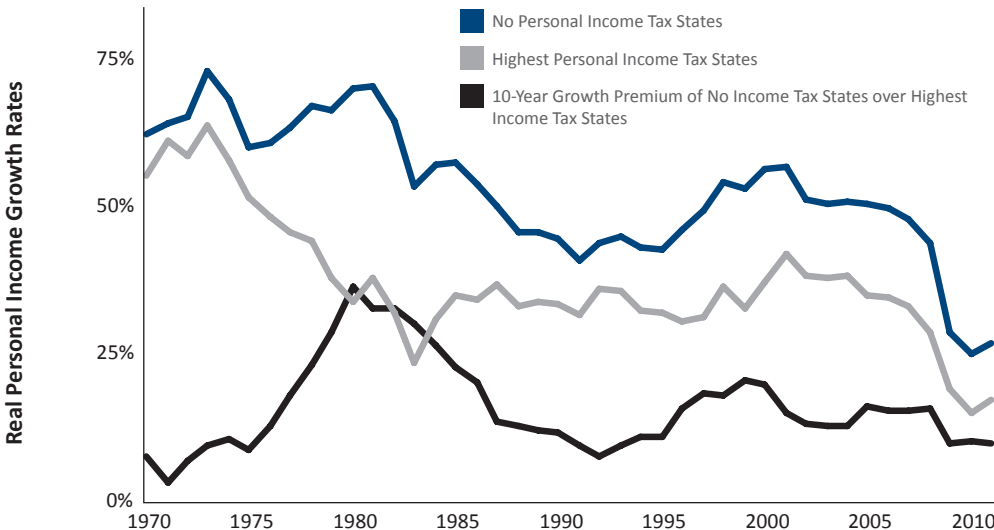
One of the most outstanding elements of the United States' system of federalism is the opportunity for states to experiment with different public policies, and for researchers of all stripes to retrospectively analyze the effect of differences in policy among the states. After all, it is notoriously tough to settle disagreements about economic policy using only theory or intuition. Moreover, the scientific method requires experimentation to confirm or disprove competing hypotheses. After decades of experimentation with different tax regimes in these state "laboratories of democracy," the results are in: Despite a steady stream of

junk economics out of various progressive think tanks, it is clear that the states embracing low or no income taxes outperform the states embracing high and inefficient taxation.

To demonstrate this, we have examined the evidence for more than two decades, with data going back to 1960, and have found that in any 10-year period, the states without an income tax consistently outperform the highest income tax states (see Figure 5).

The evidence only begins with income growth. For example, from 2001 to 2011, the average of the nine states without income taxes—Alaska, Florida, Nevada, New Hampshire, South

FIGURE 5 | 10-Year Real Total Personal Income Growth Rates for No Income Tax States, Highest Income Tax States, and Growth Premium for No Income Tax States
(Annual personal income deflated with GDP price index, 1970 to 2011)



Source: Bureau of Economic Analysis, Laffer Associates

Table 5 | 9 No Income Tax States vs. 9 Highest Income Tax States

Growth Rates, 2001-2011

States	Population	Gross State Product	Nonfarm Payroll Employment	State & Local Tax Revenue†
9 States with No Income Tax*	15.00%	63.50%	12.70%	76.30%
U.S. Average**	9.50%	51.40%	7.60%	49.80%
9 States with Highest Personal Income Tax Rates*	6.00%	45.20%	4.90%	47.90%

Source: Bureau of Economic Analysis, U.S. Census Bureau, Bureau of Labor Statistics, Laffer Associates

*Equal-weighted average

**Equal-weighted average, does not include Washington, D.C.

†2000–2010 (2011 data not yet available)

Dakota, Tennessee, Texas, Washington, and Wyoming—had 15.0 percent growth in population. Compare this to the 9.5 percent population growth rate for all states, and only 6.0 percent for the nine highest income tax states—Oregon, Hawaii, New Jersey, California, New York, Vermont, Maryland, Maine, and Ohio. The massive disparity in inter state migration represents a national referendum of sorts, as citizens vote with their feet and depart to states that best service their interests. If one was wondering what motivated this mass movement of citizens, they might look to the large gap in job growth performance between states with these different tax regimes. The nine states without an income tax experienced 12.7 percent job growth, versus 7.6 percent in the average state and 4.9 percent in the highest tax states. On balance, no income tax states have 2.5 times the population growth of the highest income tax states. Further, evidence indicates that the no income tax states have higher tax revenue growth than the national average *and* the highest income tax states.

The California/Texas comparison is especially eye-popping and illustrates the case quite clearly. California has the highest income tax rate, at 13.3 percent, and Texas has no income tax. Over the 10-year period from 2001 to 2010, Texas gained nearly 870,000 net migrants from other states, while California lost more than 1.5 million net residents to other states. Texas' gains and California's losses are nowhere more apparent than in the U.S. Census results for the 2010 congressional

reapportionment: Texas increased its congressional delegation by four seats, and for the first time in the state's history, California did not gain any seats. Yet the politicians in Sacramento sponsored a ballot initiative that passed last fall that will, retroactive to Jan. 1, 2012, increase the top tax rate from more than 10 percent to more than 13 percent—the highest in the nation.

But one need not take our word on this economic performance discrepancy between states with no income taxes and those with high income taxes. Two recent surveys of professional economic studies on taxes and economic growth have illustrated that the vast majority of economic theory and peer-reviewed quantitative analysis shows a strong connection between good tax policy (i.e., low tax burdens and taxation on consumption, not income) and economic growth. Citing studies from a range of reputable sources, including President Barack Obama's own former chair of the Council of Economic Advisers, Dr. Randall Pozdena and Dr. Eric Fruits highlight the wealth of historical evidence in agreement with the theoretical case.¹ This evidence establishes the proven negative effects of taxation on economic growth and investment. This includes national level studies, as well as those studies that analyze state level difference in tax policy and economic performance.

Similar to the efforts of Dr. Pozdena and Dr. Fruits, Dr. William McBride at the Tax Foundation analyzed the evidence regarding how taxes affect economic growth in a study titled "What

is the Evidence on Taxes and Growth?”² Dr. McBride’s findings are substantial:

“In this review of the literature, I find twenty-six such studies going back to 1983, and all but three of those studies, and every study in the last fifteen years, find a negative effect of taxes on growth. Of those studies that distinguish between types of taxes, corporate income taxes are found to be most harmful, followed by personal income taxes, consumption taxes and property taxes.”

Perhaps most staggering is the size of the effect of taxes on GDP. Christina Romer, a former chief economic adviser to President Obama, along with her husband David Romer, found that:

- Each 1 percent increase in taxation lowers real GDP by 2 to 3 percent.
- These damaging effects on the economy are persistent, and are not diminished by offsetting changes in prices.
- Investment falls sharply in response to tax increases. It is very likely that this strong retreat of investment is part of the reason that the declines in output are so large and persistent.

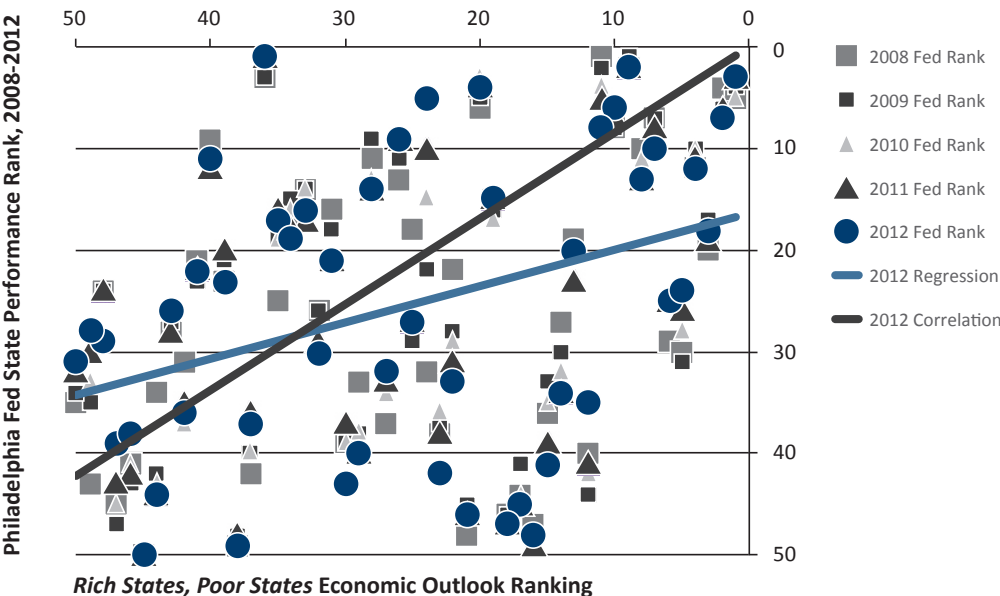
The methodology of *Rich States, Poor States* acknowledges these research insights and weighs sound tax policy heavily in its ranking of

state economic prospects. Unsurprisingly given this basis in economic theory and practice, *Rich States, Poor States* is found to heavily correlate with state economic performance. Using the Federal Reserve Bank of Philadelphia’s indices of state economic health, Dr. Fruits and Dr. Pozdena compare *Rich States, Poor States* rankings to economic outcomes. The results are clear: There is a strong, positive economic relationship between having a higher ranking in *Rich States, Poor States* and having higher economic performance.

Based in part on these powerful results, which have been replicated by numerous economic studies,³ many states, including Nebraska, North Carolina, and Louisiana, are considering abolishing their income taxes in order to accelerate growth. Now the Left is fighting back.

Recently, analysis has been published and then relentlessly republished by progressive think tanks attacking the conclusions and methodology of *Rich States, Poor States*, particularly regarding tax and budget policy. A study by the Left-leaning Institute on Taxation and Economic Policy (ITEP) challenges our conclusion that state taxes impact population, job, and income growth.⁴ The ITEP researchers find that from 2001 to 2010, “residents of high rate income tax states are actually experiencing economic conditions at least as good, if not better, than those

FIGURE 6 | Higher ALEC-Laffer Ranks Are Associated with Higher State Performance Ranks



living in states lacking a personal income tax.” ITEP goes on to reject our findings by writing that “the growth of states lacking an income tax is no more than coincidental.”⁵

Key to ITEP’s findings is the improper use of economic statistics adjusted for population when comparing state performance. Although per-capita figures can be useful for some purposes, when comparing the performance of different state tax regimes, these population adjustments are heavily distorted by inter state migration. As such, they hide the effect of unemployed or underemployed “economic refugees” fleeing high tax states for their job-creating counterparts. ITEP is not unaware of the effect of migration, but when noting the mass movement of citizens, it conveniently refuses to acknowledge the impact of public policy on migration patterns. Instead, ITEP’s assumptions largely reduce the motivations of those Americans deciding to relocate to only the desire for warmer weather and better public services.

Similar Left-wing critiques from Prof. Peter Fisher, writing for both the Iowa Policy Project and Good Jobs First and the Center for Budget and Policy Priorities (CBPP), repeat these misunderstandings of state economic performance data. Prof. Fisher’s critique, unimaginatively titled, “Selling Snake Oil to the States,” takes this problematically adjusted state performance data and purports to show that a higher ranking in *Rich States, Poor States* does not correlate with higher economic performance. CBPP’s study essentially repeats the findings of Prof. Fisher and ITEP. After citing Fisher and ITEP, CBPP goes on to suggest without evidence that businesses actually prefer robust public services to a more hospitable business climate, and vaguely asserts that “expert consensus” disagrees with the conclusions of *Rich States, Poor States*, while only citing as evidence studies of academics affiliated with left-wing think tanks, like Prof. Fisher, ITEP, and past CBPP studies.

What these studies have in common is a misunderstanding or general avoidance of economic theory, a general misuse and misinterpretation of economic data, and a firm bias in favor of big government, public sector labor unions, and redistribution over economic growth and entrepreneurship. Careful and dispassionate analysis shows what common sense already suggests: Those

states that embrace a hospitable business climate see high income growth, more job creation, higher tax revenue growth, and a diaspora of citizens flocking to the opportunity that free markets and limited government provide.

The Proof Is in the Numbers: Responding to the Critics

Clearly, there are many factors that influence economic growth. Surely, however, if location A lowers its tax rates and location B raises its tax rates, with other things being equal, businesses, capital, and people will migrate from B to A. In other words, businesses, capital, and people will move to a place with lower taxes. After all, common sense suggests that businesses, investors, and citizens who are seeking to enhance their bottom line will seek to minimize their expenses to the extent possible, and taxes (particularly on income) are fundamentally an expense that lowers the return to productive activity.

ITEP’s researchers cherry-pick data from the nine no income tax states and the nine highest income tax states. Even though state tax rates are enormously powerful drivers of growth, it only stands to reason that some of the highest income tax states will sometimes—by chance, or as a result of other factors—outperform some of the no income tax states. For example, factors such as an energy or agricultural boom or bust, or increases in military spending that disproportionately benefit states like California and Virginia, muddy the economic record with what is known as “compensating differentials.” They do not, however, eliminate the negative effect of taxes, instead only mask it. Put differently by way of metaphor, it is true that some individuals with a poor diet will outlive some who eat healthy. If you were a betting person, though, you would quickly figure out that healthy eaters, on average, are much healthier than are unhealthy eaters. Similarly, no income tax states are far more likely to achieve prosperity than are high tax states.

The six-page ITEP analysis fails to refute the fact that the no income tax states, on average, have higher, and in some cases substantially higher, growth rates in population, employment, tax revenues, and gross state product (GSP) over the past half-century than the highest income tax states. That is because this is an indisputable fact.

Population Metrics

One of the primary flaws with ITEP's analysis is its suggestion that we should "control for population growth" ostensibly because they claim that "population growth... is decidedly not determined by state tax structures." This argument defies basic common sense, and makes one wonder whether ITEP's researchers have ever chatted with a business owner or glanced at a corporate income statement and noticed taxes as an expense item. Moreover, to make a stark comparison, what if one state had a 100 percent income tax and another state had a 0 percent income tax? Undoubtedly, every single worker, entrepreneur, and investor has a certain level of taxation at which they would find circumstances unbearable and instead head to greener pastures.

Population growth differences among the states are precisely the key metrics that taxation and other state policies really impact. Ignoring population growth differences among the states when analyzing state economic policies is akin to conducting a study on the causes of obesity while ignoring whether people maintain an unhealthy diet. In the exact same sense that poor diet causes obesity, higher tax rates cause slower population growth and slower economic growth. Migration patterns between states also reveal much about where Americans think prosperity is happening and where it is not. Factors such as weather do not completely explain migration patterns between states. People are not moving out of Buffalo, NY, Detroit, MI, and Newark, NJ, because it is cold. Families moved to those cities for opportunity, and they are largely leaving for lack of opportunity.

By examining all the economic variables on a per-person basis—i.e., controlling for population growth—ITEP tries to refute our findings. However, this is an inappropriate statistical trick meant to fool non-experts. Both population and gross state product (GSP), as ITEP points out repeatedly, grow much faster in no income tax states. Therefore, when examining GSP per capita, the numerator and denominator (total GSP and population, respectively) are both growing faster in no income tax states, and it is impossible to determine whether GSP per capita should rise or fall. Sometimes population will grow

faster than the rise in GSP, and at other times it will not. Given the obsession with per-capita metrics demonstrated by ITEP and other critics, we are surprised that they do not examine per-capita growth in population. Nevertheless, whatever may happen on a per-person basis, states with low tax rates attract more people, jobs, and income than do states with high tax rates.

One of our most vocal opponents, Prof. Mickey Hepner, said, "I don't know about you, but if we have two million more people move to Oklahoma and we are poor as a result, I don't think that's progress, I don't think we're better off."⁶ Of course, the problem with this statement is that it clearly misses the point of migration. Two million people would not choose to move to Oklahoma in the first place if they became poor as a result. To the contrary, they came to Oklahoma for economic opportunity—and those citizens, along with the state as a whole, are better off because of the relocation.

Moving is costly, and building new social ties in a new community is difficult—people do not move to a new place to be poor in a different environment. That is why, when citizens are polled on their reasons for moving, the most frequently cited reasons are jobs and economic opportunity.⁷ Thus, not only are some citizens, businesses, and investors making a direct decision to move to a state with a more hospitable business climate, but many workers are indirectly voting with their feet for lower tax states by moving to the states that provide the greatest opportunity for employment and wage growth.

Further, the residents of a state can be better off even if that state's per-capita or median income decreases. If, for example, 50,000 low income agriculture workers move into Texas, those workers' incomes almost surely rise (or else they would not have moved there). The residents and business owners in Texas who benefit from their labor services are better off, and the final result is that no one is worse off. But the per-capita income in Texas may actually go down if the low-income agricultural workers earn less than the state's average wage.

This is not to say that those citizens migrating away from high tax states have lower income than those citizens migrating to high tax states. As noted in chapter 2, the average income of citizens migrating away from California is higher

than the average income of citizens migrating to California. This means there is an income premium among migrants flowing out of the state. This is a similar pattern for the other states with high income taxes. But this pattern of income migration should not be confused as a point that detracts from the fact that migration is raising per-capita income in high tax states. The average income of outbound migrants, though higher than their inbound counterparts, is still generally lower than the average income of citizens of these high tax states. This does not preclude a solid segment of very wealthy individuals fleeing a given high tax state's progressive income tax, but instead that there are enough low income individuals to pull the average income of migrants down below the state average.

So, you may ask, what *does* account for population growth differentials, according to ITEP?

Some of the explanations by the ITEP study border on the absurd. For example, the ITEP analysts conclude that the reason population growth is higher in no income tax states is because they are in the South or in the West, and have higher birth rates and Hispanic immigration. Other absurdities for population growth include "accessible suburbs."⁸ There is no mention of taxes, spending, right-to-work laws, or welfare generosity.

To quote ITEP, "Demographers have identified a large number of reasons for the population growth occurring in the South and West that are completely unrelated to these states' tax structures. Lower population density and more accessible suburbs are important factors, as are higher birth rates, Hispanic immigration, and even warmer weather."⁹ Admittedly, taxes are not alone in explaining migration patterns among states, however, the reasons ITEP gives for population growth are, at best, lazy and convenient to their ideological biases. At worst, they amount to the academic version of malpractice.

Another argument used by our critics is that most of the growth we are capturing in our studies is in the southeastern region of the country. The ITEP analysts then go on to say that people are moving to states like Florida, Georgia, Tennessee, and Texas solely for the warm weather and "the sun," as they flee the cold northeastern states. ITEP argues that it is just a "coincidence" that the low and no income tax states are in the

South, and the high income tax states are in the Northeast. Tax rates, they say, do not explain the migration patterns.

There is no doubt that a lot of people move to Florida and Georgia for the nice weather and beaches. These and other reasons are clearly factors that make these states desirable locations. We have even heard that a big factor behind the rise of population growth in the South is air conditioning, and we do not doubt there is more than a kernel of truth to that. Yet this again should lead one to ask why people moved to states with such inhospitable weather in the first place, and why there is such a sudden shift in apparent preferences for climate.

Moreover, one obvious problem with explanations relying on weather patterns is that they do not explain why New Hampshire experiences more economic growth than Vermont, or why Nevada outperforms its neighbors, or why Washington performs better than Oregon, or why Tennessee has a better economic record than Kentucky. Perhaps most baffling, it does not explain why one of the states with the nicest year-round weather—California—is experiencing significant out-migration. It does not explain why Alaska, South Dakota, and Wyoming have seen big population gains—their weather is hardly comparable to warm Southern states.

There are many factors that influence migration, including the desire to reduce one's tax burden, the search for employment by the unemployed, and the prospect of wage growth in a new position. Contrary to ITEP's assertions, we take a humble approach: Taxes and other government policies are not all that matters to migration, but they certainly matter in a significant way.

West Virginia and Nevada: A Case Study in Why Not to Rely Solely On Per-Capita Measures

The inherent problem with measuring GSP or income on a per-capita basis is plainly visible when you examine two polar-opposite states: Nevada and West Virginia. Although the comparison is but one case study, analyzing the two states offers a detailed example of the critical flaw of ITEP's analysis, and is representative of the problem as a whole. First, think of Nevada—a no income tax state that, over the decade 2001

to 2010, has ranked first in population growth, eighth in GSP growth, eighth in personal income growth, and ninth in non-farm payroll employment growth.

Nevada has been a magnet for people, jobs, and output for years, gaining another congressional seat during the 2010 reapportionment. Nevada has also been extremely attractive to foreign immigrants, who usually have incomes below the average of native Nevadans. This is all the more impressive when one considers that Nevada, led by Las Vegas and Reno, was one of the states hit the hardest by the housing crisis coinciding with the recent economic recession.¹⁰ Nevada is a remarkable story of resilience and, better, economic flourishing in the face immense adversity.

Foreign immigration is certainly good for immigrants, because they are likely able to enjoy higher wages and a higher standard of living. Foreign immigration is also a boon for native Nevadans, who enjoy all of the benefits from an inflow of lower cost, high quality labor. However, according to ITEP's and others' preferred metric, Nevada ranked 48th in per-capita personal income growth and 35th in median household income growth from 2001 to 2010.

On the other hand, take a state like West Virginia, which ITEP ranks first in median household income growth from 2001 to 2010. West Virginia has gone from comprising 0.79 percent of the nation's total personal income in the five years before it introduced a personal income tax in 1961, to comprising only 0.48 percent of the nation's personal income as of 2011. One certainly would not consider these metrics of West Virginia to be the components of a prosperous state. People, jobs, and income have been fleeing this state for a very long time, although the recent development of the Marcellus shale oil field in towns like Wheeling are attracting rapid development as we speak.

ITEP's measure of West Virginia's and Nevada's prosperity is telling after further investigation. One important point to understand about changes in median income is to recognize that a state's median income is the income of the middle worker, where half of the people earn more and half of the people earn less. Median income will rise if low income workers lose their jobs or leave the state, which is what happened

in West Virginia. Median income will fall if a large number of low income workers find jobs, which has been demonstrated in Nevada.

West Virginia has experienced the polar opposite of Nevada. Over the past several decades, West Virginia's able-bodied lower and middle class workers have been unable to find work in West Virginia, and have fled the state in search of opportunities. Lower income residents are leaving the state more rapidly than higher income residents. As a result, West Virginia has experienced a rise in median income. As the state continues to fall behind in terms of economic competitiveness, some wealthy families choosing to remain in West Virginia despite its dysfunctional public policy represent a statistical rise in median household income growth.

It seems that neither Nevadans nor foreign immigrants mind the state's lackluster per-capita ranking, given that Nevada continues to attract both Americans and foreign immigrants in droves. Nevada's low median household income growth and low per-capita personal income growth are the result of an increased amount of employment opportunities for low income earners.

Instead, we argue that population growth is a highly revealing metric of future prosperity. People make the decision whether or not to move, and tax rates affect those decisions. People vote with their feet and generally do not migrate to places where they will be worse off. History has demonstrated this notion to be true over and over. People migrated from East Germany to West Germany, North Korea to South Korea, Mexico to the United States—not in search of better weather, but in search of freedom, opportunity, and an increased standard of living.

A simple question puts the immigration issue in perspective: Would you rather have people lined up on your state's border trying to add the talent and productive capabilities to your state, or instead face the prospect of scores of economic refugees trying to leave?

Finally, while it is true that per-capita GSP *levels* are generally higher in the high income tax states—like New York, California, and New Jersey—on the contrary, it is false that per-capita GSP *growth* is consistently higher in those states. After examining 40 years of data, it has become apparent that, at times, the no income tax states grow faster in GSP and jobs *per capita*, and at

other times they do not, largely for the reason discussed above. For example, between 2001 and 2010, per-capita GSP grew 37.2 percent in the no income tax states, and just 33.4 percent in the high income tax states.

Reverse Causation and Population

Another refutable argument put forth by ITEP and other critics of our work is that people move from one place to another for sunshine or no particular reason, and, of course, they take their incomes with them as a tagalong. This is precisely what ITEP argues.¹¹ ITEP further surmises that, after sensing the coming prosperity, the states' legislatures and governors cut their states' tax rates. By this logic, it is future prosperity that causes current tax cuts, not the reverse.¹² ITEP argues that this is why we find a "spurious correlation" between growth rates and taxes.

In the words of Prof. Hepner, "the relationship is presumed to be changes in taxes lead to or determine the change in income levels, but in reality what we saw in the 1980s was just the opposite ... Again, it's not the tax cuts that led to the growth, it's the growth that led to the tax cuts."¹³

Hepner's comments imply that the government raises tax rates during weak economic times, and cuts tax rates during times of strong economic growth. Not only is this contrary to the logic of any school of economics we have ever seen—you cannot tax an economy into prosperity—but it is also contrary to the facts. President Ronald Reagan cut tax rates in the heart of a recession/depression. President John Kennedy cut tax rates in the worst period of a recession. President Warren Harding also cut tax rates at the bottom of an economic cycle.

On the state level, we have seen many examples of states that cut taxes during tough economic times and grew their economies. The state of Michigan has demonstrated this result over the last 30 years. The state was experiencing a mini-depression in the early 1990s, and, even in the midst of this economic crisis, then-Gov. John Engler cut tax rates more than at any time in the history of Michigan. The economy of this Rust Belt state boomed as a result for most of the 1990s, and even at one point had an unemployment rate below the national average. After Engler left office, his successor, Jennifer Granholm, raised

taxes, and the long and deep slide that Michigan is experiencing now began anew. The same result was demonstrated in New Jersey. The economy was in collapse in the early 1990s after James Florio raised taxes. Gov. Christine Whitman cut tax rates by more than 20 percent, and New Jersey went through a mini-boom and retained a budget surplus.

Presidents Herbert Hoover and Franklin Roosevelt raised tax rates in a depression. The sluggishness of the recovery from the Great Depression is well documented. President Obama is trying his level best to follow in Hoover's and Roosevelt's footsteps. When President Bill Clinton raised income tax rates, we were already well into a boom, and thus his policy was the beneficiary of slightly muted economic consequences.

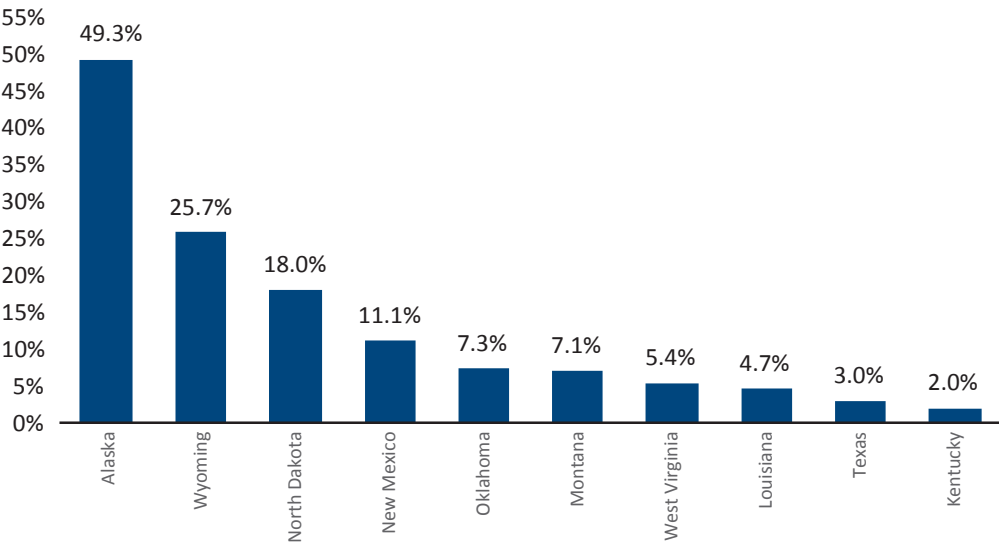
According to ITEP's logic, passage of Proposition 13 in California in 1978 would have to have been the direct consequence of a vision of the 1980s future prosperity by the state's clairvoyant legislators, led by then-optimistic Gov. Jerry Brown. Today in California, now led by a pessimistic Gov. Jerry Brown, a new batch of clairvoyant state politicians foresee their own state's demise and are thus raising taxes.

Oil, Sunshine, and Prosperity

Our critics say we fail to account for "oil and sunshine." In all of our work, we have specifically taken into account all sorts of other factors including oil and, yes, even sunshine. This critique was addressed directly in the fifth edition of *Rich States, Poor States*.¹⁴ Even if the two states with the highest oil severance tax revenue—Alaska and Wyoming—are eliminated from the comparison of no income tax states with an aggregate of all states and a grouping of the highest tax states, the seven remaining no income tax states still outperform the U.S. average and significantly outperform the highest income tax states in growth of income, employment, and population. Even in the past, when there was an oil bust and oil prices fell, the no income tax states, including the oil states, outperformed both the national average and the highest tax states (see Figure 5).

We acknowledge that factors such as oil and sunshine do indeed have an impact on state economic growth. For example, North Dakota's population and economy is booming today,

FIGURE 7 | Top 10 Severance Tax States as a Percentage of Total State and Local Tax Revenue (2001-2010)



Source: U.S. Census Bureau

not solely because of its tax code, but also because it has massive amounts of new natural gas and oil operations. Our rebuttals to our critics' oil comments notwithstanding, our detractors still persist in arguing that no income tax states tend to be energy-rich states—like Alaska, Texas, and Wyoming—and that the resources they retain explain why no income tax states are doing well. If true, then our critics should explain the performances of New Mexico, Oklahoma, Montana, West Virginia, and Louisiana, all of which

have more oil severance tax revenue than Texas (Figure 7).

The 11 States that Adopted an Income Tax

Our most conclusive test to account for a whole host of other factors was examining what happened to the 11 states that introduced an income tax over the past half-century, before and after its implementation. To be precise, in each

Table 6 | Economic Consequences from the Introduction of the State Income Tax

States	Share of Total U.S. GDP	Share of Total U.S. Population	Share of Total U.S. State Tax Revenue
11 States, Average of 5 Years Prior to Income Tax Introduction*	33.00%	31.00%	27.80%
11 States in 2011†*	22.50%	23.10%	24.60%
Change	-10.50%	-7.90%	-3.20%

Source: Bureau of Economic Analysis, U.S. Census Bureau, Laffer Associates

†"Share of Total U.S. State Tax Revenue" is from 2010 due to data limitations.

* The 11 states are CT, NJ, OH, RI, PA, ME, IL, NE, MI, IN, and WV. Because of GSP data limitations, West Virginia's economic activity is measured as a share of national personal income.

case here we examined the exact same state before it had an income tax and after it adopted an income tax, using a long-run window that minimizes the impact of the 2007–2008 fiscal downturn. We look at each state’s share of total U.S. GSP and population for the average of the five years prior to the introduction of the state’s income tax, and then for the most recent year, 2011.

To quote from *Eureka!*, “What we find absolutely astonishing is how the size of the economy in each one of these states has declined as a share of the total U.S. economy compared to a time just

prior to when each state introduced its income tax. Some of the declines are quite large.”¹⁵ Needless to say, ITEP and our other critics never mention this result, which has been displayed prominently in our publications. (See Table 6.)

ITEP’s analysts would perhaps argue that these 11 states—Ohio, Michigan, Maine, West Virginia, Pennsylvania, Illinois, Indiana, Connecticut, New Jersey, Rhode Island, and Nebraska—have all of a sudden gotten a lot cloudier and run out of oil reserves. ITEP’s criticisms and excuses aside, what the data clearly shows is that 11 states that have adopted an income tax have

Table 7 | 22 Right-to-Work States vs. 28 Forced Union States*
Growth Rates, 2001-2011

States*	Gross State Product	Population	Nonfarm Payroll Employment	Personal Income
22 Right-to-Work States*	59.20%	13.10%	11.20%	56.90%
50 State Average**	51.40%	9.50%	7.60%	49.40%
28 Forced Union States*	45.20%	6.80%	4.80%	43.60%

*Equal-weighted average; IN and MI were not included as RTW states because the law had not passed in these states during this time period.

**Equal-weighted average; does not include D.C.

Source: Bureau of Economic Analysis, U.S. Census Bureau, Bureau of Labor Statistics, Laffer Associates

Table 8 | 9 States with Lowest Transfer Payments vs. 9 States with Highest Transfer Payments

States	2010	Growth Rates, 2001-2011			
	Welfare Spending Per Person in Poverty (end of period)†	Gross State Product	Population	Non-Farm Payroll Employment	Personal Income
9 States With Lowest Welfare Payments Per Person in Poverty*	\$6,533	55.00%	16.60%	12.10%	52.90%
50 State Average**	\$11,589	51.40%	9.50%	7.60%	49.40%
9 States With Highest Welfare Payments Per Person in Poverty*	\$19,423	44.70%	5.40%	4.60%	43.10%

† “Public Welfare” from Census Bureau State & Local Government Finances per person in poverty. The table uses 2010 figures because of data limitations.

*Equal-weighted average

**Equal-weighted average; does not include D.C.

Source: U.S. Census Bureau, Bureau of Economic Analysis, Bureau of Labor Statistics, Laffer Associates

faced economic decline—or, at least, been outpaced by the rest of the 39 states in terms of economic growth.

Other Economic Factors Our Critics Overlook

Other key factors that ITEP fails to take into account in its focus on oil, sunshine, and reverse causality are what we have found to be other important growth factors: right-to-work states outperform closed-shop or forced union states (Table 7); states with high transfer payments (cash or programmatic benefits like health care, paid directly to a citizen) per eligible person also have lower growth (Table 8); estate and corporate

taxes and overregulation also negatively affect growth.¹⁶ Despite the importance of these aspects, ITEP fails to mention them even though they have been shown repeatedly to be key factors in determining growth.

IRS Data, Moving Van Data, and State Migration

We have examined Internal Revenue Service (IRS) and Census Bureau data covering at least two decades regarding people who move from one state to another. Looking at the past six years' worth of data—from 2004–2005 to 2009–2010—we have identified the number of tax filers who moved specifically from the nine highest

Table 9 | IRS State to State Migration Data*

States	Sum, 2004–2005 to 2009–2010		2004–2005 to 2009–2010
	Aggregate Adjusted Gross Income (\$000,000s)	# of Returns Filed	Average Adjusted Gross Income Per Filer
Filers in the 9 No Income Tax States Who Previously Filed in the 9 Highest Income Tax States	\$72,857.70	1,325,374	\$54,971.43
Filers in the 9 Highest Income Tax States Who Previously Filed in the 9 No Income Tax States	\$39,523.11	909,176	\$43,471.35
Net Difference	\$33,334.59	416,198	\$11,500.08

Source: Internal Revenue Service, Laffer Associates

* One year's worth of IRS migration data are created by matching individual tax returns from one year with the next year. For example, the first year in the sums above, 2004–2005, comes from filers' 2004 returns matched with those same filers' 2005 returns.

Table 10 | United Van Lines Migration Data
2007–2011

States	Inbound Shipments	Inbound as a % of Total	Outbound Shipments	Outbound as a % of Total
8 No Income Tax States*	204,072	53.00%	180,638	47.00%
8 Highest Income Tax States**	197,155	47.70%	216,469	52.30%

Source: United Van Lines, Laffer Associates

*The table contains data for 8 states rather than 9 because United Van Lines does not ship to Alaska.

**The table contains data for 8 states rather than 9 because United Van Lines does not ship to Hawaii.

tax states to the nine no income tax states, as well as their aggregate adjusted gross income and the average income per filer. Additionally, we have identified the same data for filers who moved from the nine no income tax states to the nine highest tax states.

By now, it should come as no surprise that far more tax returns—416,000 more—are from people moving to the no income tax states from the highest income tax states than the reverse. Moreover, the average adjusted gross income of those moving to the no income tax states is far higher than is the average adjusted gross income of those moving from the no income tax states to the highest income tax states. The data shows clearly that Americans are packing up and moving into low tax states and taking their incomes along with them (Table 9).

We have also examined the United Van Lines data on where people move from and where they move to. Low tax states are huge net destination points, and high tax states are population repellants. (Tables 9 and 10.)

In fact, reflecting net migration patterns, the rates of moving van companies such as U-Haul are at times far lower for the few people who use these moving van companies to move to a high tax state like California from a low tax state like Tennessee. In 2008, for example, the cost to rent a full-sized U-Haul truck to move from Los Angeles, CA, to Nashville, TN, was \$4,285—more than six times the \$557 cost of moving in the opposite direction. Similarly, it cost \$4,254 to rent a full-size truck from Los Angeles, CA, to Austin, TX, yet only \$407 for the reverse trip. In 2012, it cost \$2,312 to rent a U-Haul truck from Trenton, NJ, to Houston, TX, but only \$905 going the opposite way; Philadelphia, PA, to Nashville, TN, costs \$1,380, but Nashville, TN, to Philadelphia, PA, costs only \$788.¹⁷

Price data does not lie: Citizens are voting with their feet and choosing those states that have embraced competitive tax policy. Similarly, the extensive research by Travis Brown in his book *How Money Walks*, along with recent research by scholars at the Mercatus Center, demonstrates that migration has an unmistakable connection to public policy. Freedom ushers in opportunity and ambitious citizens move to chase opportunity.¹⁸

Addressing Other Criticisms of Pro-Growth Tax Reform

Our critics also say that federal tax rates matter more than state tax rates because federal rates are significantly higher. For some purposes, this may well be true. However, just because federal tax rates have a greater impact on the U.S. economy than state tax rates, it does not mean that state rates do not matter. In fact, conceding that federal tax rates matter guarantees that state tax rates also matter. Regardless of who levies them, taxes have the same effect on behavior.

Prof. Hepner referred earlier to the idiosyncrasies of federal tax codes to argue that income and property taxes should be used more and not less because they are deductible on federal tax returns. Perhaps this provision is why New York, California, Vermont, and New Jersey are not performing even more poorly. It is true that federal tax policy rewards states for raising their income taxes by allowing these state taxes to be deducted from federal taxes. But it is also true that state sales taxes paid can also be deducted from federal taxes, a fact Prof. Hepner seems to ignore. We make the argument that the deduction for both income and sales taxes should be eliminated, because it simply serves as a subsidy for irresponsible state tax policy. It is not fair that residents in a low income tax state, one that is fiscally responsible and spends its money wisely (say, New Hampshire), have to pay more income taxes than someone of equal income from a high income tax state (say, California) that squanders resources.

It is additionally worth considering the hypocrisy and bizarre logic of the Left's position on state taxes. For instance, consider that one reason the Left wants the federal government to give tens of billions of dollars to states for hiring teachers and firefighters and for building roads, rather than states raising and spending the money themselves, is that they know that interstate economic competition precludes states from raising their own taxes significantly. Some on the Left derisively call this the "race to the bottom." Why, though, would they characterize this as a tax-cutting race to the bottom if they actually believe that taxes do not affect behavior and migration?

Or consider another example: The Left has been arguing for a long time—and so have many

large retailers—that Internet sales by remote sellers should be forced to collect sales taxes because people will buy things on the Internet and avoid paying their state use tax on the items. If taxes do not affect behavior, why should it matter? Interestingly, states have tried to persuade the federal government to require all states to tax Internet purchases so that the states that do impose those taxes are not losing firms and sales to states that do not. Why do high tax states like New York, California, Illinois, New Jersey, and others spend so much tax enforcement money trying to find out whether high income residents spend 183 days in Florida or Tennessee to avoid income taxes? If income taxes do not matter, why would people try to pretend that they live in no income tax states?

Based on economics, an important reason why the income tax should be eliminated rather than eliminating other taxes is that the income tax directly impacts the marginal or incremental incentive to work and innovate. No other major state tax has anything like the marginal impact of an income tax. On a dollar-for-dollar basis, taxes on income and capital are far and away the most damaging taxes to output, employment, and production.¹⁹

Changing tax rates is all about economic dynamics and incentives. People are averse to doing things that they find disadvantageous, while people like doing things that they find attractive. Taxes make an activity less attractive, and, therefore, encourage people to do less of that activity. If government taxes people for working and pays people not to work, do not be surprised if more people choose not to work.

When it comes to the poor, the minorities, and the disadvantaged, incentives matter as much as they do for anyone else. Taxing the rich and giving the money to the poor will increase the number of poor people and reduce the number of rich people. The dream in America has never been to make the rich poorer. It has always been to make the poor richer. The best form of welfare is a good, high-paying job, and the “least-worst” tax for creating jobs is a low rate flat tax on consumption.

To all of this, Prof. Hepner responded with a curious argument, borrowing from Sen. Elizabeth Warren. Hepner said:

“[T]he wealthy don’t become wealthy

on their own. They became wealthy as part of a system, as a part of a country that supported and educates its populace, that provides roads, that allows commerce to take place, that supports the infrastructure of the city, the state and this nation.”²⁰

Hepner goes on to say that the wealthy owe their success to government, and should therefore pay higher tax rates.

The first logical fallacy with Hepner’s inference from an obviously correct observation is that government did not provide the “system” of resources, the taxpayers and the private sector did. The second fallacy is his inference that not everyone had an equal chance to use all of the resources our society provided. Those resources were provided for everyone, not just for those people who used them well. As a result, there is no reason why those who used our publicly available resources well should be required to pay disproportionately more than those people who did not use them as effectively. This then leads to the third fallacy of making those who successfully use our publicly available resources pay disproportionately more. Levying greater taxes on the people who successfully use our publicly available resources will only assure less aggregate wealth and progress for future generations—i.e., fewer publicly available resources in the future.

ITEP and others point out that the progressive state income tax takes away from those who can most afford to pay taxes, and that any cut in the income tax would “shift the tax burden away from the highest earning people ... to more on the backs of the lower-income and middle class families.”²¹ This argument, used by Hepner and all opponents of income tax cuts, is called the “reverse Robin Hood” effect. As we have tried to explain, progressive income taxes fail to redistribute income, but instead effectively redistribute people. Advocates of progressive income taxes also ignore that the central goal of tax policy should be to grow total wealth while funding the core functions of government, not redistribute current wealth or enrich special interests.

Federal tax codes are generally quite similar in all 50 states, but state and local tax codes can be substantially different from state to state.²² Therefore, if someone is going to move from one

state to another for tax reasons, it seems clear that state and local taxes should be the deciding factor. It is easier for a business or family to move from one state to another than from one country to another.²³

Responding to CBPP and Peter Fisher

In addition to the criticisms of ITEP, Professor Peter Fisher, on behalf of both the Iowa Policy Project and Good Jobs First, and the Center for Budget and Policy Priorities (CBPP), have both written critiques of our policy recommendations in *Rich States Poor States*, and called into question the performance of those states implementing these common-sense reforms. While claiming to share concerns for state business climate competitiveness, these groups, much like ITEP, are primarily focused on maintaining the status quo of government spending (particularly spending related to public employee unions) and all of their papers emphasize this central goal. The errors of their policy analysis are worth considering in this light.

Prof. Fisher, in a paper titled “The Doctor is Out to Lunch” and then updated as “Selling Snake Oil to the States,” takes the central premise of ITEP’s work—states that implement *Rich States, Poor States*’ policy recommendations perform more poorly than those states that do not—and purports to use statistical methods to show the same conclusion as ITEP, but with even greater methodological rigor.²⁴ Though using higher-powered statistical methods is certainly a fruitful exercise in settling this debate, Prof. Fisher’s methodological errors prevent his analysis from making any substantive contribution to the debate. As one reviewer put it, Fisher’s analysis is “simplistic, unprofessional, and technically flawed—but well promoted.”²⁵

Fisher’s first error is a familiar one—he considers per-capita income growth, instead of absolute growth rates. As discussed extensively throughout this publication, this ignores the impact of migration, which in large part is affected by a state’s business climate, including tax and regulatory policy. Moreover, even Fisher’s own analysis finds that those states that embrace sound economic policy consistent with *Rich States, Poor States* see substantially higher population growth, therefore tacitly acknowledging that citizens are “voting with their feet” for economic freedom.

Additionally, Fisher only looks at those years between 2007-2011. This narrow time range introduces substantial statistical bias by virtue of it covering a mere five years of data. Moreover, this time range coincides with a massive economic recession, which further skews and biases the economic data due to the prevalence of irregular and unprecedented economic phenomena. Based on these two errors alone, Fisher’s analysis is doomed to imprecision and “spurious” findings.

But the errors of Fisher’s analysis do not stop with time concerns and the use of per-capita data. Dr. Eric Fruits and Dr. Randall Pozdena offered a thorough critique of Fisher’s work and found even deeper concerns with his methodology.²⁶ First, they critique Fisher’s choice to use *shares* of employment in various sectors of the economy as bizarre, unorthodox, and ultimately incorrect. They note that this is akin to “trying to explain one measure of growth with another measure with no attempt to demonstrate which one is the cause of the other.” In terms of statistical analysis of economic questions, this is essentially a deathblow to professional research.

Second, Dr. Fruits and Dr. Pozdena find that Prof. Fisher ignores the litany of research that finds a strong connection between tax policy and economic health once other factors besides tax policy that affect growth are accounted for properly. Fisher’s models include no “control variables.” This means that in his model of the economy, he fails to consider every other common and accepted variable affecting economic health, instead only analyzing taxes, right-to-work policy, and the *Rich States, Poor States* index as the sole determinants of economic health. Failing to include the appropriate control variables in a statistical analysis introduces further statistical bias.

Third and finally, Fisher uses the wrong measures of economic health, and considers raw numbers instead of *rankings*. *Rich States, Poor States*, being a ranking of economic policy, must be compared against a comparable ranking. After critiquing Prof. Fisher’s research, Dr. Fruits and Dr. Pozdena perform the correctly specified statistical tests and find that the rankings in *Rich States, Poor States* do indeed correlate with rankings of economic health. Using the Federal Reserve Bank of Philadelphia’s indices of state

economic health, they find the strong and positive relationship detailed in Figure 6. These results prove the obvious—those states that embrace a healthy business climate experience a more healthy economy.

Moreover, in a separate paper recently published, Dr. Fruits and Dr. Pozdena find that right-to-work, a policy also maligned by Fisher, is a strong predictor of economic health.²⁷ After pointing out that 8 of the 11 credible academic studies of right-to-work labor policies and state economic health have shown right-to-work states outperform compulsory union states, Dr. Fruits and Dr. Pozdena perform an independent analysis. They find a strong positive connection between employment growth (particularly employment in manufacturing), state personal income growth, wage and salary growth, and net migration growth.

A separate analysis by CBPP essentially rehashes the flawed analysis of ITEP and Prof. Fisher, and asserts academic consensus regarding the irrelevance of tax policy and right-to-work policy on academic health. To assert this consensus, CBPP largely cites its own scholars, along with Prof. Fisher and scholars from other center-Left think tanks like ITEP or the Economic Policy Institute. In doing so, CBPP ignores the actual consensus of the academic literature on these topics, as previously discussed in this chapter. Economic theory and the historical record show that economic freedom matters immensely to economic health.

CBPP rounds out their faulty analysis by arguing that what economists and business leaders say really matters to economic health are public services, not a state's business climate. The consensus of economists has already been discussed on this matter, but it is worth briefly noting that the National Federation of Independent Business, the primary trade association for small business, surveys its own members on what matters most to them.²⁸ These results show CBPP is far off the mark—a simple review of business leaders stated priorities shows clearly that business climate, and not public services, is what matters to business growth and, in turn, economic growth.

The studies published by Prof. Fisher and CBPP, much like the studies penned by ITEP, are done in what appears to the naive consumer of

economic research to be credible and professional analysis, but ultimately add confusion and distortion, not insight, to the debate on state economic policy. These studies are all well promoted and shared through the center-Left echo-chamber with impressive vigor and efficiency. But their prevalence is no indicator of their accuracy, and they are indeed incorrect. These groups would be better suited by arguing for the value of spending programs over and above their tax cost and economic cost, given that spending is their ultimate priority, rather than distorting the economic record on what truly matters to economic health.

Conclusion

To end this discussion, we believe that it is important for ITEP and other critics to consider the findings from our studies. For us, if the nine no income tax states consistently underperformed the nine highest tax states once all appropriate factors were accounted for, the very foundation of our beliefs would be shaken. If each of the 11 states that adopted income taxes increased their economic health relative to the rest of the nation with all elements considered, we would certainly reconsider our policy prescriptions. Though we, along with most, absolutely value freedom for freedom's sake, and feel that liberty is both of instrumental and intrinsic value, we ultimately are guided by facts and the goal of improving social welfare. We reject ideology and dogma.

Not only does the state data confirm our view of the world, the relationships between country growth rates and country economic policies also confirm our worldview. Time series of countries and time series of states also show the same results. Studies and examples of specific states and specific taxes further confirm our view.

Our state analysis is intended to help advise lawmakers on the best pro-growth policies to help their citizens. They cannot, alas, change the weather or where their state is located, or have much of an impact on how much oil they have in the ground. They can however, change their taxes, the amount that state and local governments spend, whether their state has right-to-work laws, and how generous their state's welfare system is. The quality of schools also matters, as does the state's highway system. It takes years, though, for those policies to pay dividends, while

cutting taxes can have a near-immediate and permanent impact. This is why we think Oklahoma, Kansas, and other states should cut their income tax rates if they want the most effective immediate and lasting boost to their states' economies.

ITEP inadvertently seems to concede the broader point that we have made for years, that the Northeast is becoming like Europe and the economic gazelles in the U.S. are in the South. We have always argued that it is not only tax rates that matter. Government spending matters, the level of regulation matters, and whether the state has a right-to-work law matters. The Northeast is losing ground to the South because it has much more government control of the economy than do the Southern states. It is not an accident that the auto industry has left the Midwest for the South. There are numerous examples of this, including Airbus opening up its new plant in the South.

Much of the Northeast and Midwest are falling further and further behind, while the South, along with much of the Plains and Mountain states, are booming. One of the biggest factors behind that phenomenon is that these areas, on a wide variety of economic policy variables that we have examined, are the fastest growing and most economically healthy regions of this country. They are much more receptive to business and worker rights than the high tax, heavily unionized Northeast. The future is happening in the low tax South and Great Plains, while high tax California, New York, and Illinois are increasingly looking like the Greece of North America.

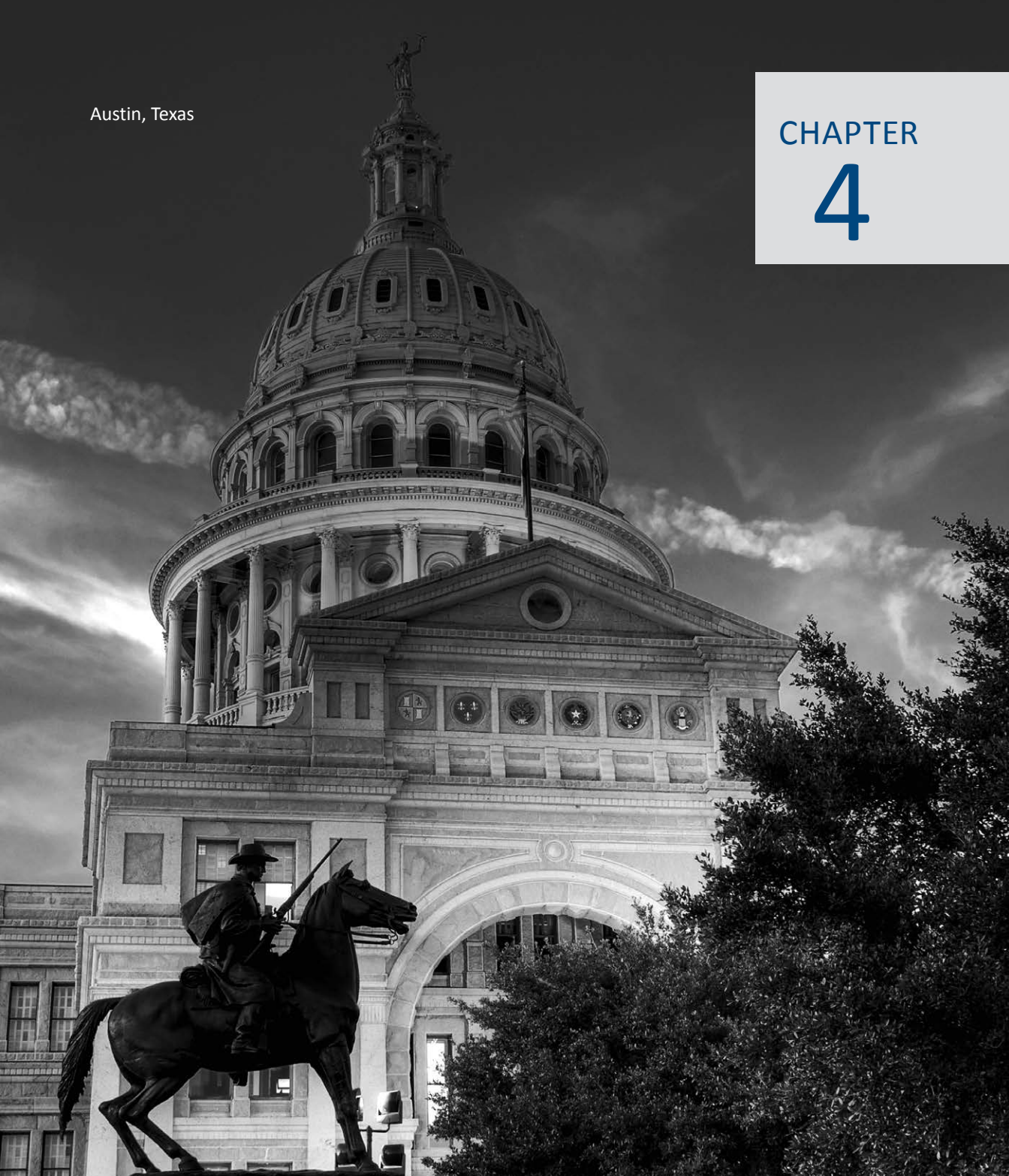
In the face of the overwhelming body of evidence we have presented, we ask ourselves, is there any amount of disconfirming data that would ever cause these people to change their minds? This chapter represents our efforts to test our critics' intellectual honesty.

(ENDNOTES)

- 1 Fruits, Eric and Pozdena, Randall. "Tax Myths Debunked." American Legislative Exchange Council. February 2013.
- 2 McBride, William. "What Is The Evidence on Taxes and Growth?" Tax Foundation. December 18, 2012.
- 3 Laffer, Arthur B. and Winegarden, Wayne H. "State Economics: Who Has the Facts?" Laffer Associates. February 21, 2012.
- 4 "'High Rate' Income Tax States Are Outperforming No-Tax States." Institute on Taxation and Economic Policy. February 2012. See also, "States with 'High Rate' Income Taxes are Still Outperforming No-Tax States." Institute on Taxation and Economic Policy. February 28, 2013.
- 5 "States with 'High Rate' Income Taxes are Still Outperforming No-Tax States." Institute on Taxation and Economic Policy. February 28, 2012.
- 6 Hepner, Mickey. "Tax Policy Forum [Video Recording]." State Chamber of Oklahoma. May 9, 2012.
- 7 Schachter, Jason. "Why People Move: Exploring the March 2000 Current Population Survey." U.S. Census Bureau. May 2011. See also, Cohn, D'Vera. "American Mobility: Who Moves? Who Stays Put? Where's Home?" Pew Research Center. December 29, 2008.
- 8 "'High Rate' Income Tax States Are Outperforming No-Tax States." Institute on Taxation and Economic Policy. February 2012.
- 9 *Ibid.*
- 10 Brenna, Morgan. "2010's Worst Cities for Foreclosures." *Forbes*. January 26, 2011.
- 11 "'High Rate' Income Tax States Are Outperforming No-Tax States." Institute on Taxation and Economic Policy. February 2012.
- 12 Hepner, Mickey. "Tax Policy Forum [Video Recording]." State Chamber of Oklahoma. May 9, 2012.
- 13 *Ibid.*
- 14 Laffer, Arthur B., Moore, Stephen, and Williams, Jonathan. *Rich States, Poor States: ALEC-Laffer State Economic Competitiveness Index*, 5th edition. The American Legislative Exchange Council. April 2012.
- 15 Laffer, Arthur B. and Winegarden, Wayne H. "Eureka!: How to Fix California." Pacific Research Institute. March 2012.
- 16 Laffer, Arthur B. and Winegarden, Wayne H. "The Economic Consequences of Tennessee's Gift and Estate Tax." The Laffer Center for Supply-Side Economics and Beacon Center of Tennessee. March 2012.
- 17 U-Haul price data were collected from www.uhaul.com.
- 18 Ruger, William and Sorens, Jason. "Freedom in the 50 States." The Mercatus Center at George Mason University. March 2013.
- 19 For literature review on topic, see: Fruits, Eric and Pozdena, Randall. "Tax Myths Debunked." American Legislative Exchange Council. February 2013. Also, see: McBride, William. "What Is The Evidence on Taxes and Growth." Tax Foundation. December 18, 2012.
- 20 Hepner, Mickey. "Tax Policy Forum [Video Recording]." State Chamber of Oklahoma. May 9, 2012.
- 21 "'High Rate' Income Tax States Are Outperforming No-Tax States." Institute on Taxation and Economic Policy. February 2012.
- 22 Not surprisingly, federal taxes can vary across states even when the federal tax codes don't change. The Alternative Minimum Tax (AMT) is much more impactful in high-tax states because state tax payments are a "preferred deduction," and therefore not allowed in the calculation of the AMT tax base. There is at least one state that allows federal taxes as a state deduction, and federal taxes allow state tax deductions if the filer itemizes.
- 23 For some people, federal taxes have become so onerous that they have renounced their citizenship specifically for tax reasons. It has lately become an issue of national concern that wealthy Americans are renouncing their citizenship and moving abroad for tax reasons. In this light, ITEP's contention that no one moves from one state to another for tax reasons is a stretch, to say the least.
- 24 Fisher, Peter and LeRoy, Greg and Mattera, Philip. "Selling Snake Oil to the States." Good Jobs First and The Iowa Policy Project. November 2012.
- 25 Fruits, Eric and Pozdena, Randall. "Tax Myths Debunked." American Legislative Exchange Council. February 2013.
- 26 Fisher, Peter and LeRoy, Greg, Mattera, Philip. "Selling Snake Oil to the States." Good Jobs First and The Iowa Policy Project. November 2012.
- 27 Fruits, Eric and Pozdena, Randall. "Right To Work is Right for Oregon." Cascade Policy Institute. February 2012.
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Austin, Texas

CHAPTER
4



State Rankings

State Rankings

The Economic Outlook Ranking is a forecast based on a state’s current standing in 15 state policy variables. Each of these factors is influenced directly by state lawmakers through the legislative process. Generally speaking, states that spend less—especially on income transfer programs, and states that tax less—particularly on productive activities such as working or investing—experience higher growth rates than states that tax and spend more.

The Economic Performance Ranking is a backward-looking measure based on a state’s performance on three important variables: State Gross Domestic Product, Absolute Domestic Migration, and Non-Farm Payroll Employment—all of which are highly influenced by state policy. This ranking details states’ individual performances over the past 10 years based on this economic data.

Table 11 | ALEC-Laffer State Economic Outlook Rankings, 2013

Based upon equal-weighting of each state’s rank in 15 policy variables

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

Table 12 | **ALEC-Laffer State Economic Performance Rankings, 2001-2011**

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

Alabama

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

30

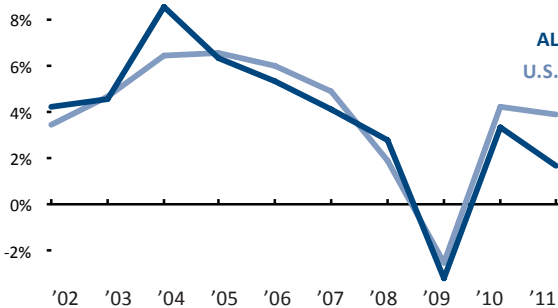
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

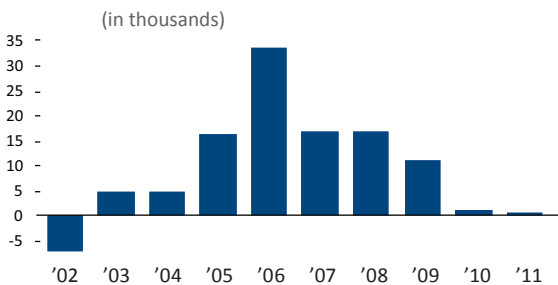
State Gross Domestic Product

Cumulative Growth 2001-2011 44.1% Rank: 32



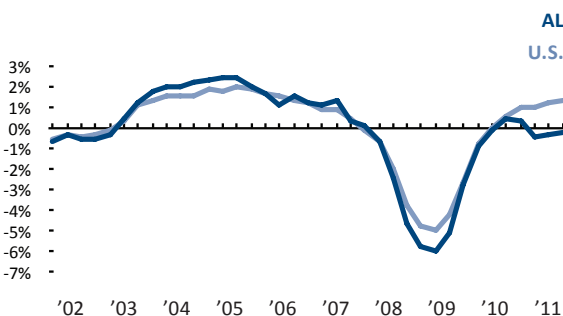
Absolute Domestic Migration

Cumulative 2002-2011 97,417 Rank: 14



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 -1.5% Rank: 37



17

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison
ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
15 16 17 20 21

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	4.02%	12
Top Marginal Corporate Income Tax Rate	4.23%	6
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	-\$2.04	1
Property Tax Burden (per \$1,000 of personal income)	\$16.44	1
Sales Tax Burden (per \$1,000 of personal income)	\$24.80	30
Remaining Tax Burden (per \$1,000 of personal income)	\$23.06	41
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010& 2011, per \$1,000 of personal income)	-\$0.19	20
Debt Service as a Share of Tax Revenue	9.2%	32
Public Employees Per 10,000 of Population (full-time equivalent)	592.9	39
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	52.8	43
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.97	30
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	0	34

Alaska

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

8

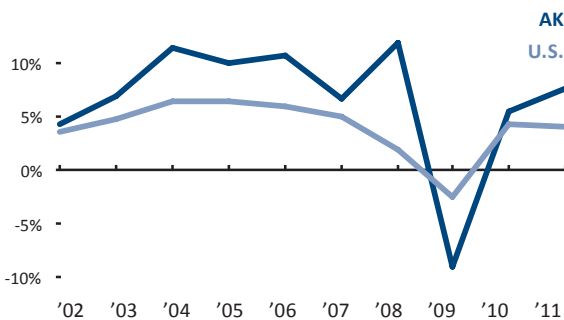
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

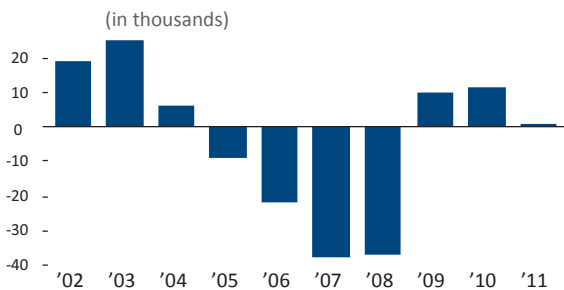
State Gross Domestic Product

Cumulative Growth 2001-2011 85.2% Rank: 3



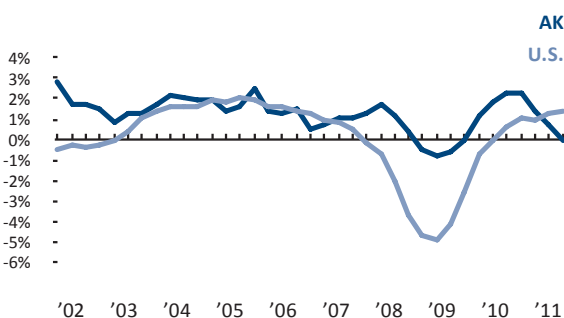
Absolute Domestic Migration

Cumulative 2002-2011 -3,154 Rank: 29



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 13.0% Rank: 4



21

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
37 38 22 29 29

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	0.00%	1
Top Marginal Corporate Income Tax Rate	9.40%	43
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$0.00	2
Property Tax Burden (per \$1,000 of personal income)	\$43.29	39
Sales Tax Burden (per \$1,000 of personal income)	\$11.22	5
Remaining Tax Burden (per \$1,000 of personal income)	\$16.70	15
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$1.59	7
Debt Service as a Share of Tax Revenue	7.0%	12
Public Employees Per 10,000 of Population (full-time equivalent)	757.5	49
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	69.1	13
State Minimum Wage (federal floor is \$7.25)	\$7.75	36
Average Workers' Compensation Costs (per \$100 of payroll)	\$3.01	50
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	1	15

Arizona

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

7

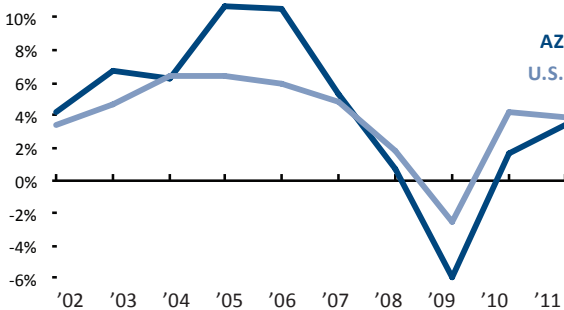
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

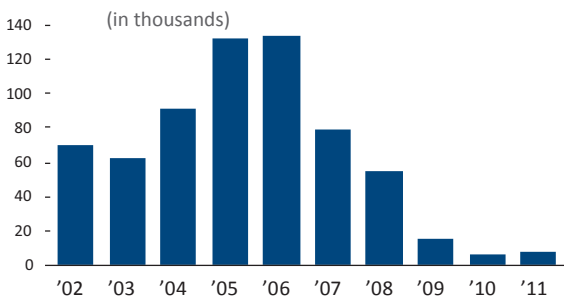
State Gross Domestic Product

Cumulative Growth 2001-2011 52.0% Rank: 21



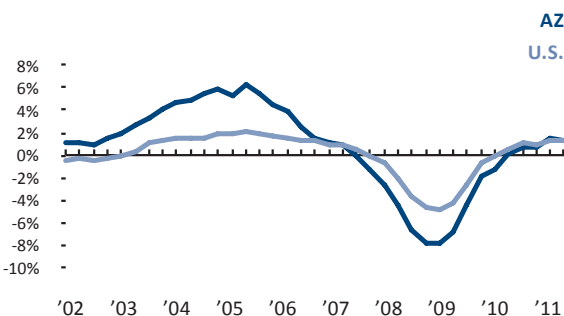
Absolute Domestic Migration

Cumulative 2002-2011 653,658 Rank: 4



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 7.3% Rank: 11



6

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison	2008	2009	2010	2011	2012
ECONOMIC OUTLOOK RANK	6	3	3	12	9

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	4.54%	13
Top Marginal Corporate Income Tax Rate	6.97%	23
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$10.55	29
Property Tax Burden (per \$1,000 of personal income)	\$34.35	26
Sales Tax Burden (per \$1,000 of personal income)	\$31.06	41
Remaining Tax Burden (per \$1,000 of personal income)	\$13.33	5
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010& 2011, per \$1,000 of personal income)	-\$2.84	5
Debt Service as a Share of Tax Revenue	11.6%	43
Public Employees Per 10,000 of Population (full-time equivalent)	433.2	2
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	66.8	17
State Minimum Wage (federal floor is \$7.25)	\$7.80	40
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.61	14
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	2	4

Arkansas

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

22

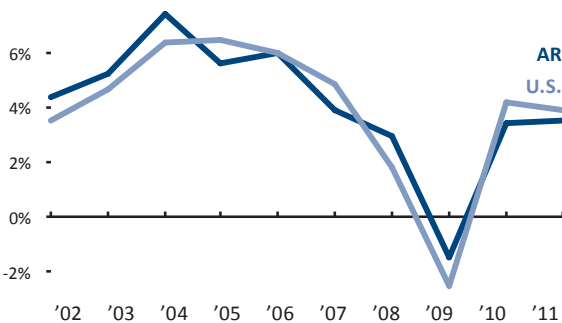
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

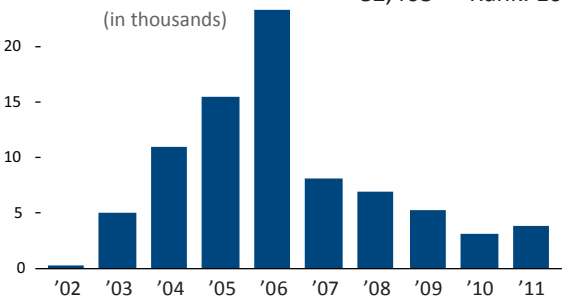
State Gross Domestic Product

Cumulative Growth 2001-2011 48.9% Rank: 25



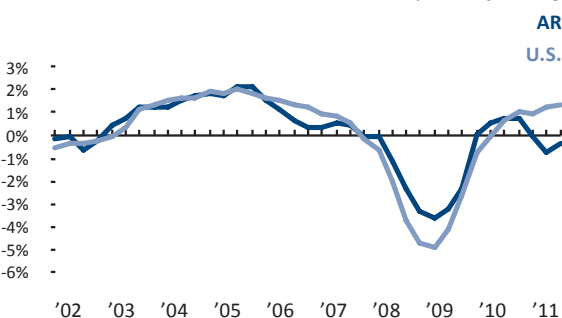
Absolute Domestic Migration

Cumulative 2002-2011 82,403 Rank: 16



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 1.1% Rank: 26



24

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
11 12 13 13 11

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	7.00%	34
Top Marginal Corporate Income Tax Rate	6.50%	19
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$14.33	39
Property Tax Burden (per \$1,000 of personal income)	\$18.81	3
Sales Tax Burden (per \$1,000 of personal income)	\$38.21	47
Remaining Tax Burden (per \$1,000 of personal income)	\$18.18	22
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$0.89	39
Debt Service as a Share of Tax Revenue	5.4%	3
Public Employees Per 10,000 of Population (full-time equivalent)	645.4	45
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	57.2	35
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.19	3
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	1	15

California

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

43

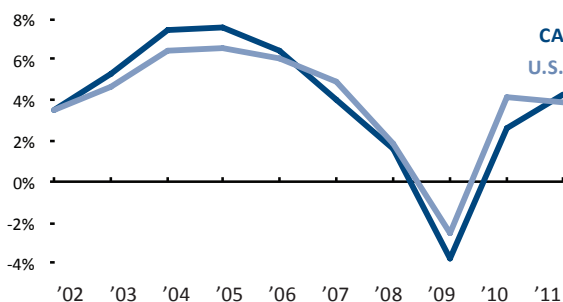
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

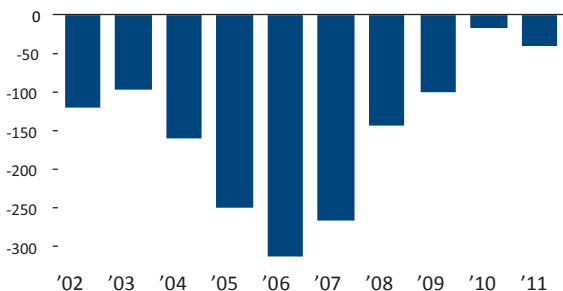
State Gross Domestic Product

Cumulative Growth 2001-2011 46.2% Rank: 27



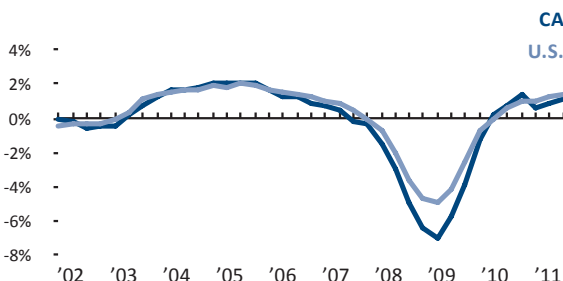
Absolute Domestic Migration

Cumulative 2002-2011 -1,503,970 Rank: 49
(in thousands)



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 -2.3% Rank: 41



47

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
42 43 46 47 38

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	13.30%	50
Top Marginal Corporate Income Tax Rate	8.84%	38
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$37.36	50
Property Tax Burden (per \$1,000 of personal income)	\$35.28	27
Sales Tax Burden (per \$1,000 of personal income)	\$26.10	33
Remaining Tax Burden (per \$1,000 of personal income)	\$15.79	12
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010& 2011, per \$1,000 of personal income)	\$0.17	33
Debt Service as a Share of Tax Revenue	10.2%	37
Public Employees Per 10,000 of Population (full-time equivalent)	464.8	5
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	50.6	47
State Minimum Wage (federal floor is \$7.25)	\$8.00	43
Average Workers' Compensation Costs (per \$100 of payroll)	\$2.92	48
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	2	4

Colorado

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

20

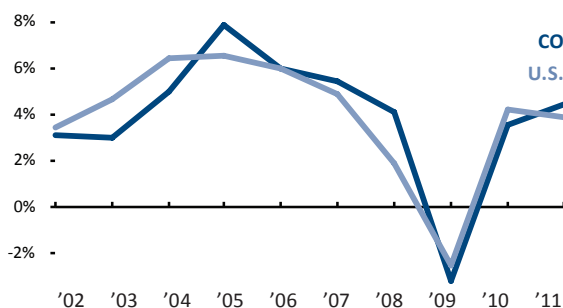
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

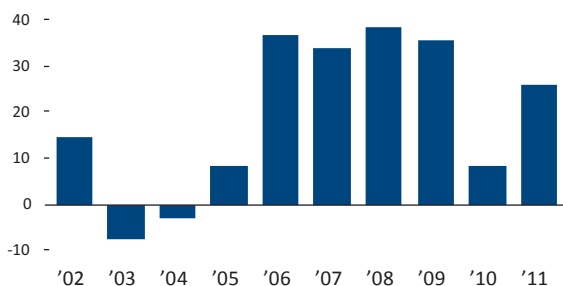
State Gross Domestic Product

Cumulative Growth 2001-2011 46.0% Rank: 28



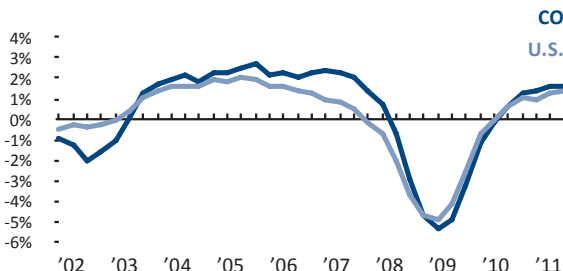
Absolute Domestic Migration

Cumulative 2002-2011 (in thousands) 191,786 Rank: 10



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 3.1% Rank: 19



16

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
9 2 2 6 8

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	4.63%	14
Top Marginal Corporate Income Tax Rate	4.63%	7
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$6.17	19
Property Tax Burden (per \$1,000 of personal income)	\$38.86	35
Sales Tax Burden (per \$1,000 of personal income)	\$24.20	28
Remaining Tax Burden (per \$1,000 of personal income)	\$14.30	7
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$0.21	35
Debt Service as a Share of Tax Revenue	12.6%	48
Public Employees Per 10,000 of Population (full-time equivalent)	528.0	23
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	64.2	23
State Minimum Wage (federal floor is \$7.25)	\$7.78	38
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.42	8
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	3	1

Connecticut

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

46

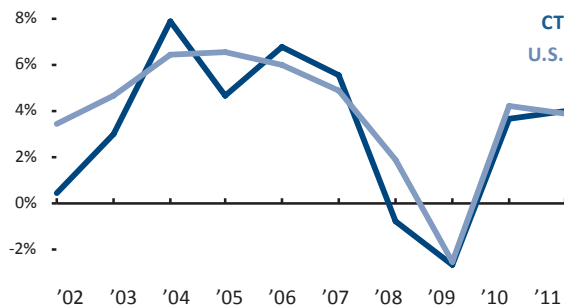
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

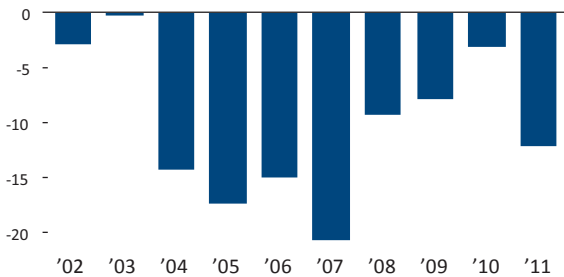
State Gross Domestic Product

Cumulative Growth 2001-2011 36.8% Rank: 45



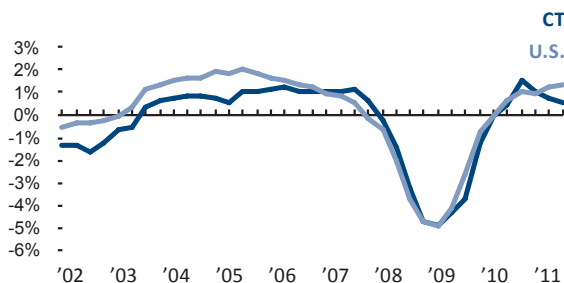
Absolute Domestic Migration

Cumulative 2002-2011 (in thousands) -102,670 Rank: 41



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 -3.1% Rank: 45



43

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
40 32 36 35 44

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	6.70%	29
Top Marginal Corporate Income Tax Rate	9.00%	40
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$7.67	25
Property Tax Burden (per \$1,000 of personal income)	\$46.92	43
Sales Tax Burden (per \$1,000 of personal income)	\$16.40	11
Remaining Tax Burden (per \$1,000 of personal income)	\$15.59	10
Estate/Inheritance Tax Levied?	Yes	50
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$8.48	49
Debt Service as a Share of Tax Revenue	8.7%	26
Public Employees Per 10,000 of Population (full-time equivalent)	517.2	17
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	63.8	25
State Minimum Wage (federal floor is \$7.25)	\$8.25	45
Average Workers' Compensation Costs (per \$100 of payroll)	\$2.99	49
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	1	15

Delaware

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

26

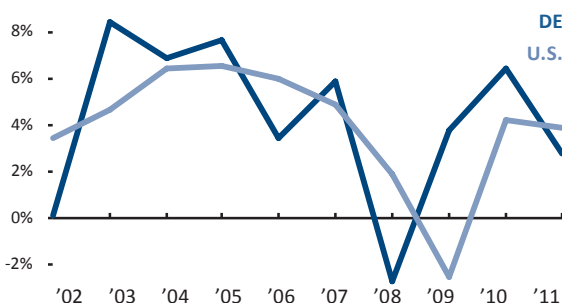
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

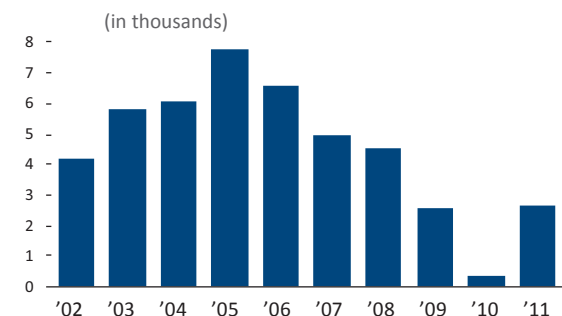
State Gross Domestic Product

Cumulative Growth 2001-2011 50.7% Rank: 22



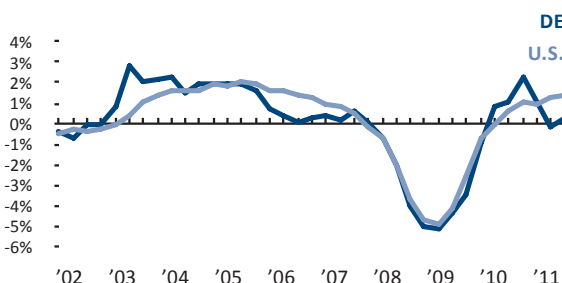
Absolute Domestic Migration

Cumulative 2002-2011 45,564 Rank: 19



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 -0.1% Rank: 34



30

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
31 31 37 34 34

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	8.00%	41
Top Marginal Corporate Income Tax Rate	10.49%	47
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$15.97	43
Property Tax Burden (per \$1,000 of personal income)	\$19.19	4
Sales Tax Burden (per \$1,000 of personal income)	\$0.00	1
Remaining Tax Burden (per \$1,000 of personal income)	\$53.72	50
Estate/Inheritance Tax Levied?	Yes	50
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$1.19	8
Debt Service as a Share of Tax Revenue	10.2%	36
Public Employees Per 10,000 of Population (full-time equivalent)	548.4	28
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	75.8	1
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.77	21
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	2	4

Florida

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

14

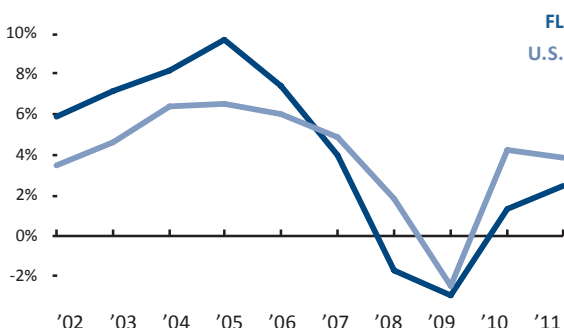
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

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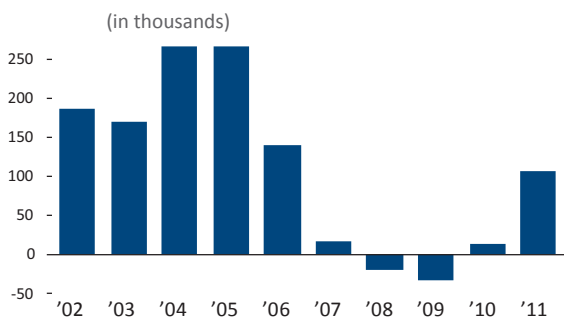
State Gross Domestic Product

Cumulative Growth 2001-2011 48.9% Rank: 24



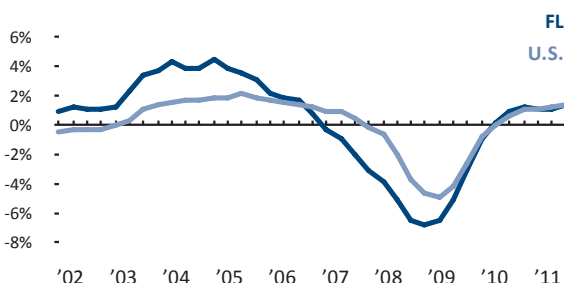
Absolute Domestic Migration

Cumulative 2002-2011 1,114,069 Rank: 1



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 2.6% Rank: 21



9

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
16 11 5 10 13

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	0.00%	1
Top Marginal Corporate Income Tax Rate	5.50%	13
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$0.00	2
Property Tax Burden (per \$1,000 of personal income)	\$40.55	37
Sales Tax Burden (per \$1,000 of personal income)	\$28.36	39
Remaining Tax Burden (per \$1,000 of personal income)	\$22.91	40
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$0.29	18
Debt Service as a Share of Tax Revenue	8.8%	27
Public Employees Per 10,000 of Population (full-time equivalent)	466.0	6
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	55.3	41
State Minimum Wage (federal floor is \$7.25)	\$7.79	39
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.82	22
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0=least/worst 3=most/best)	2	4

Georgia

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

31

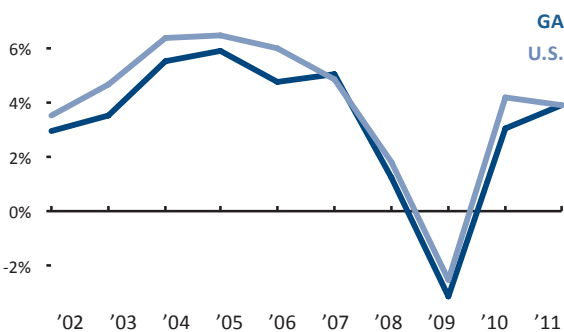
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

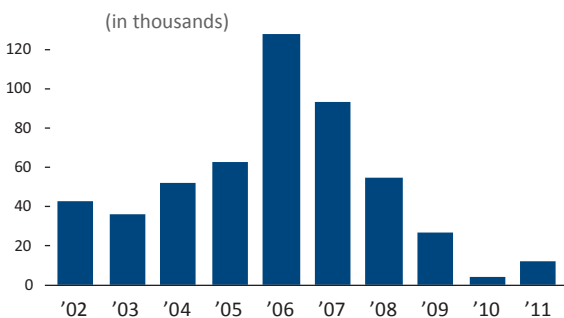
State Gross Domestic Product

Cumulative Growth 2001-2011 37.4% Rank: 44



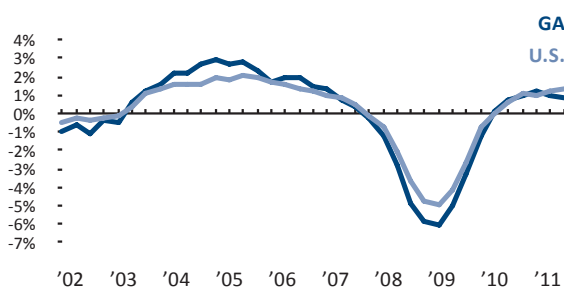
Absolute Domestic Migration

Cumulative 2002-2011 511,101 Rank: 5



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 -0.4% Rank: 35



8

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
8 8 9 11 10

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	6.00%	26
Top Marginal Corporate Income Tax Rate	6.00%	14
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$6.53	21
Property Tax Burden (per \$1,000 of personal income)	\$32.27	22
Sales Tax Burden (per \$1,000 of personal income)	\$25.39	32
Remaining Tax Burden (per \$1,000 of personal income)	\$10.60	1
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$0.19	19
Debt Service as a Share of Tax Revenue	7.3%	14
Public Employees Per 10,000 of Population (full-time equivalent)	518.9	19
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	64.0	24
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.88	24
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	0	34

Hawaii

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

17

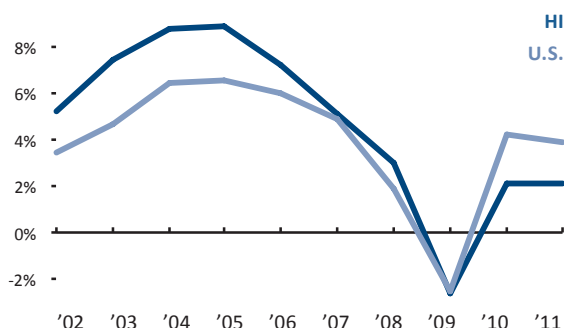
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

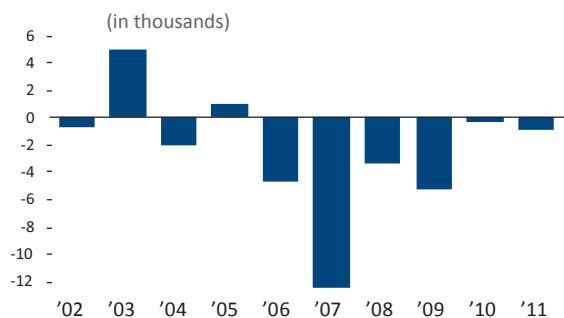
State Gross Domestic Product

Cumulative Growth 2001-2011 57.5% Rank: 15



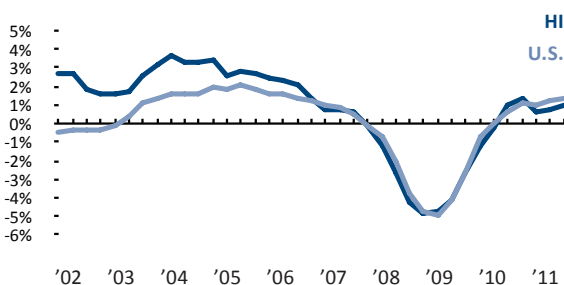
Absolute Domestic Migration

Cumulative 2002-2011 -23,721 Rank: 32



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 8.8% Rank: 7



40

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
41 41 39 46 46

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	11.00%	48
Top Marginal Corporate Income Tax Rate	6.40%	18
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$13.54	37
Property Tax Burden (per \$1,000 of personal income)	\$25.50	11
Sales Tax Burden (per \$1,000 of personal income)	\$42.40	50
Remaining Tax Burden (per \$1,000 of personal income)	\$23.47	43
Estate/Inheritance Tax Levied?	Yes	50
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$2.88	45
Debt Service as a Share of Tax Revenue	7.6%	17
Public Employees Per 10,000 of Population (full-time equivalent)	535.8	24
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	62.5	29
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.66	16
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	1	15

Idaho

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

6

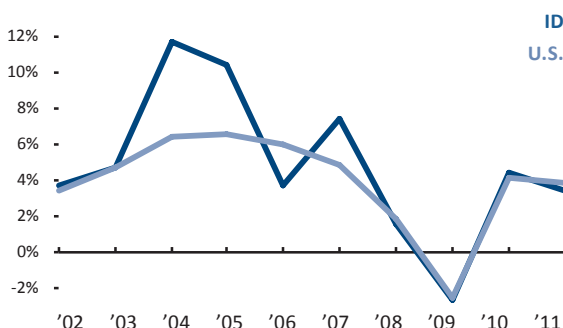
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

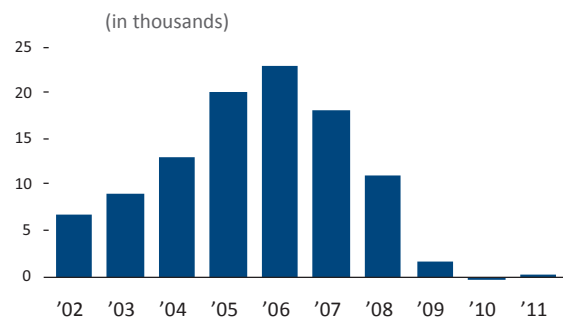
State Gross Domestic Product

Cumulative Growth 2001-2011 59.2% Rank: 11



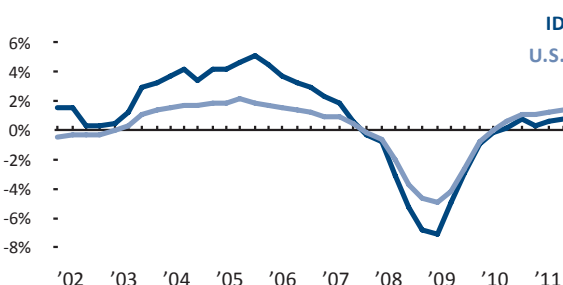
Absolute Domestic Migration

Cumulative 2002-2011 102,726 Rank: 13



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 8.0% Rank: 9



7

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
10 14 7 5 6

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	7.40%	36
Top Marginal Corporate Income Tax Rate	7.40%	26
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$12.94	35
Property Tax Burden (per \$1,000 of personal income)	\$27.03	15
Sales Tax Burden (per \$1,000 of personal income)	\$23.27	25
Remaining Tax Burden (per \$1,000 of personal income)	\$15.11	9
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$0.11	32
Debt Service as a Share of Tax Revenue	6.3%	7
Public Employees Per 10,000 of Population (full-time equivalent)	495.7	10
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	70.5	6
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$2.02	32
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	1	15

Illinois

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

47

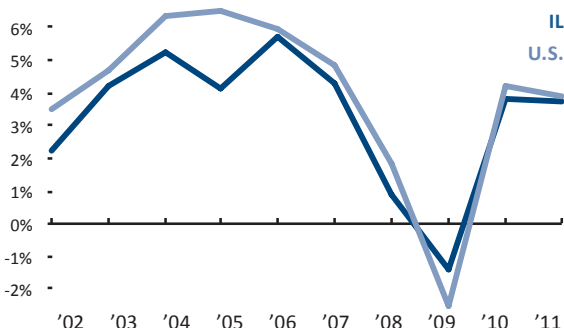
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

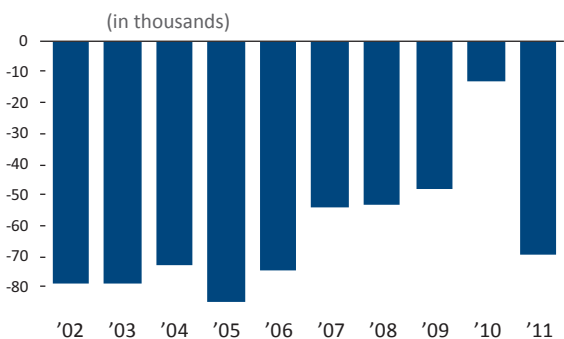
State Gross Domestic Product

Cumulative Growth 2001-2011 37.7% Rank: 42



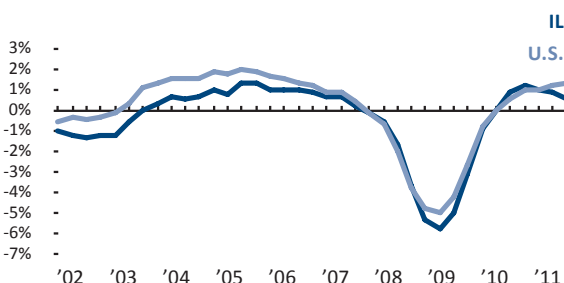
Absolute Domestic Migration

Cumulative 2002-2011 -627,630 Rank: 48



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 -4.2% Rank: 48



48

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
43 44 47 44 48

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	5.00%	17
Top Marginal Corporate Income Tax Rate	9.50%	44
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$1.33	14
Property Tax Burden (per \$1,000 of personal income)	\$44.43	41
Sales Tax Burden (per \$1,000 of personal income)	\$16.19	10
Remaining Tax Burden (per \$1,000 of personal income)	\$22.51	38
Estate/Inheritance Tax Levied?	Yes	50
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$13.86	50
Debt Service as a Share of Tax Revenue	11.6%	44
Public Employees Per 10,000 of Population (full-time equivalent)	487.1	9
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	51.3	46
State Minimum Wage (federal floor is \$7.25)	\$8.25	45
Average Workers' Compensation Costs (per \$100 of payroll)	\$2.83	47
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	0	34

Indiana

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

39

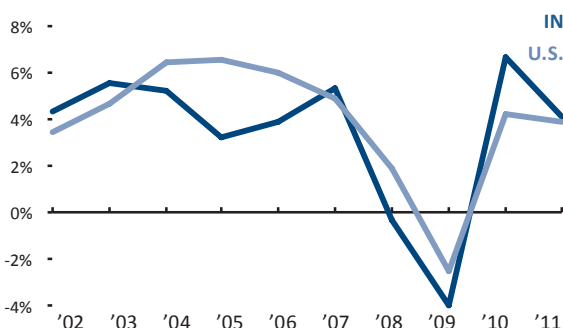
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

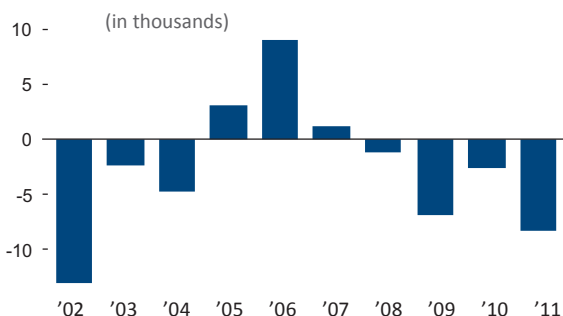
State Gross Domestic Product

Cumulative Growth 2001-2011 39.1% Rank: 38



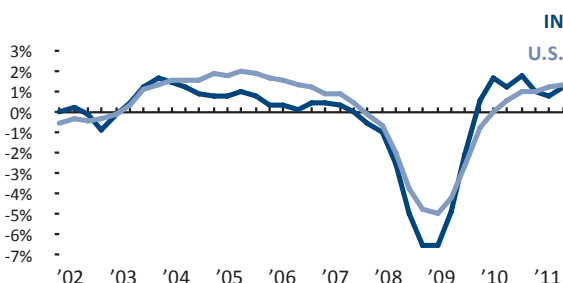
Absolute Domestic Migration

Cumulative 2002-2011 -26,033 Rank: 34



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 -2.2% Rank: 39



14

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison

2008 2009 2010 2011 2012

ECONOMIC OUTLOOK RANK

12 17 20 16 24

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	5.02%	20
Top Marginal Corporate Income Tax Rate	8.00%	32
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$0.67	13
Property Tax Burden (per \$1,000 of personal income)	\$35.38	28
Sales Tax Burden (per \$1,000 of personal income)	\$27.47	36
Remaining Tax Burden (per \$1,000 of personal income)	\$17.18	18
Estate/Inheritance Tax Levied?	Yes	50
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$1.18	41
Debt Service as a Share of Tax Revenue	9.0%	29
Public Employees Per 10,000 of Population (full-time equivalent)	505.6	12
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	69.0	14
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.16	2
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	1	15

Iowa

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

25

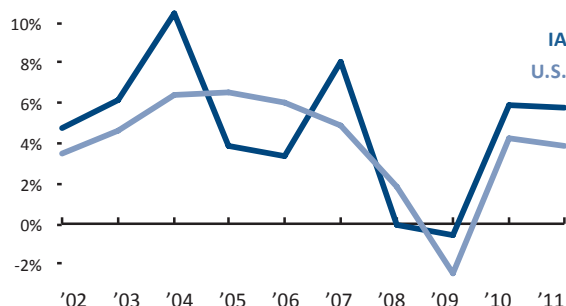
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

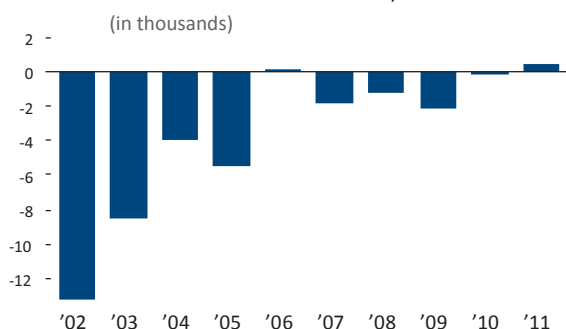
State Gross Domestic Product

Cumulative Growth 2001-2011 58.3% Rank: 13



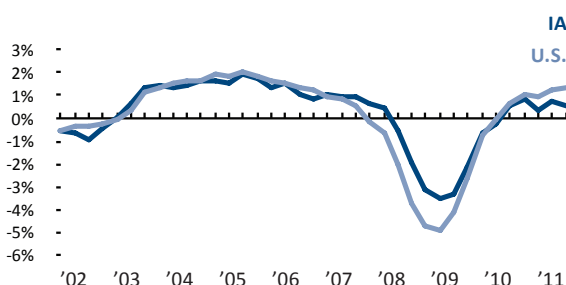
Absolute Domestic Migration

Cumulative 2002-2011 -35,983 Rank: 37



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 1.9% Rank: 24



25

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
25 35 28 23 22

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	5.42%	23
Top Marginal Corporate Income Tax Rate	9.90%	46
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$11.93	33
Property Tax Burden (per \$1,000 of personal income)	\$36.69	32
Sales Tax Burden (per \$1,000 of personal income)	\$24.16	27
Remaining Tax Burden (per \$1,000 of personal income)	\$18.63	25
Estate/Inheritance Tax Levied?	Yes	50
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$0.11	21
Debt Service as a Share of Tax Revenue	5.3%	2
Public Employees Per 10,000 of Population (full-time equivalent)	578.9	37
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	69.5	10
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.90	26
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	1	15

Kansas

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

35

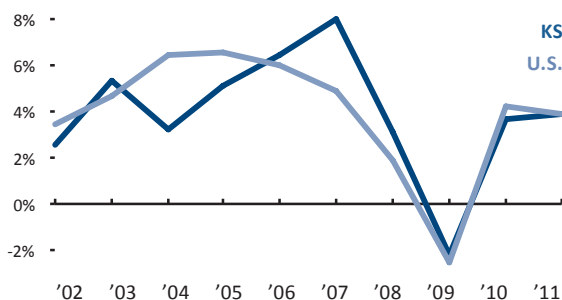
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

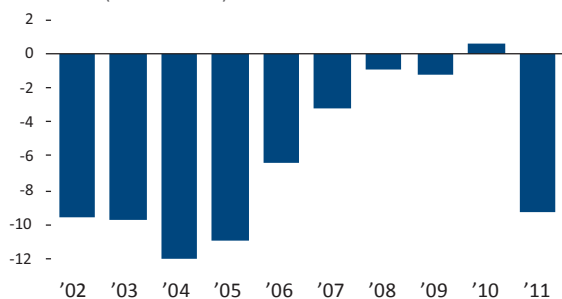
State Gross Domestic Product

Cumulative Growth 2001-2011 46.5% Rank: 26



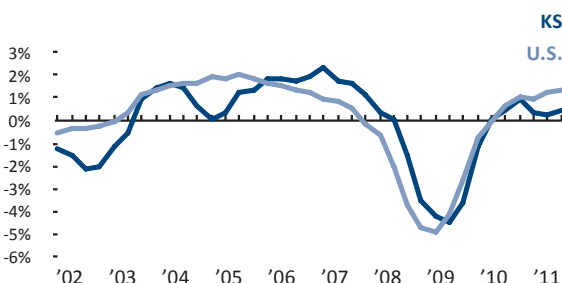
Absolute Domestic Migration

Cumulative 2002-2011 (in thousands) -62,623 Rank: 40



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 -0.6% Rank: 36



11

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
29 24 25 27 26

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	4.90%	15
Top Marginal Corporate Income Tax Rate	7.00%	24
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$7.23	23
Property Tax Burden (per \$1,000 of personal income)	\$36.42	29
Sales Tax Burden (per \$1,000 of personal income)	\$26.89	35
Remaining Tax Burden (per \$1,000 of personal income)	\$13.32	4
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$1.97	6
Debt Service as a Share of Tax Revenue	11.5%	41
Public Employees Per 10,000 of Population (full-time equivalent)	685.6	48
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	70.6	5
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.54	10
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	0	34

Kentucky

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

29

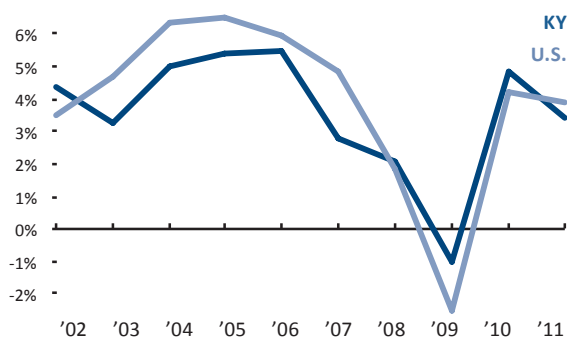
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

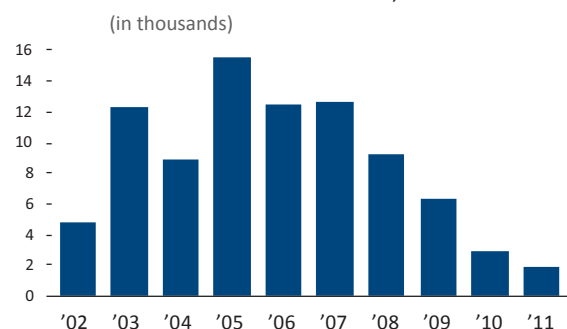
State Gross Domestic Product

Cumulative Growth 2001-2011 41.6% Rank: 36



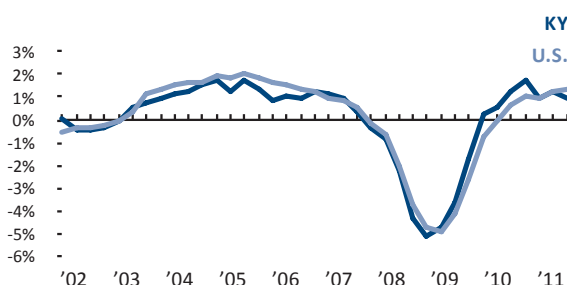
Absolute Domestic Migration

Cumulative 2002-2011 86,817 Rank: 15



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 0.7% Rank: 30



38

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
44 36 40 40 39

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	8.20%	42
Top Marginal Corporate Income Tax Rate	6.00%	14
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$5.51	18
Property Tax Burden (per \$1,000 of personal income)	\$21.37	7
Sales Tax Burden (per \$1,000 of personal income)	\$20.15	18
Remaining Tax Burden (per \$1,000 of personal income)	\$21.80	36
Estate/Inheritance Tax Levied?	Yes	50
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$0.38	36
Debt Service as a Share of Tax Revenue	13.8%	50
Public Employees Per 10,000 of Population (full-time equivalent)	565.0	33
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	56.8	38
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.96	29
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	1	15

Louisiana

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

27

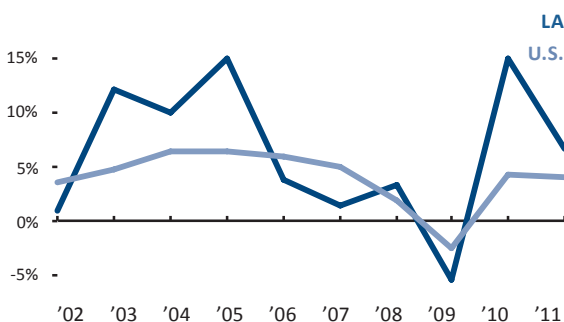
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

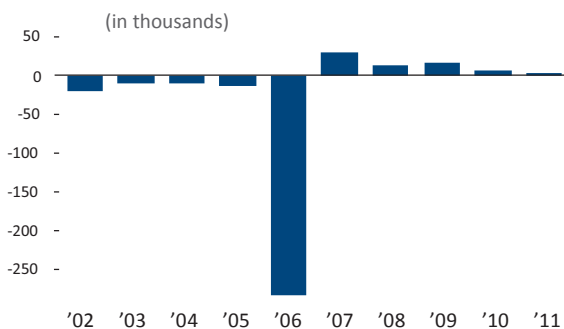
State Gross Domestic Product

Cumulative Growth 2001-2011 79.8% Rank: 4



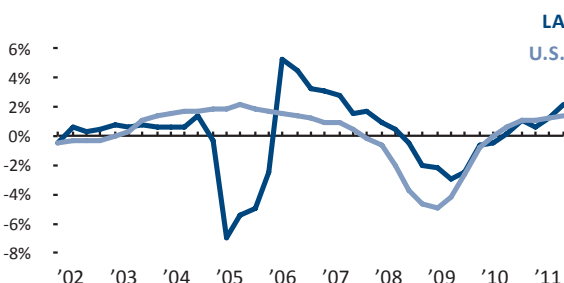
Absolute Domestic Migration

Cumulative 2002-2011 -270,251 Rank: 44



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 1.0% Rank: 28



28

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
24 18 16 15 19

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	3.62%	10
Top Marginal Corporate Income Tax Rate	5.20%	12
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$10.21	27
Property Tax Burden (per \$1,000 of personal income)	\$20.66	6
Sales Tax Burden (per \$1,000 of personal income)	\$37.50	46
Remaining Tax Burden (per \$1,000 of personal income)	\$19.52	28
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$0.00	26
Debt Service as a Share of Tax Revenue	11.6%	45
Public Employees Per 10,000 of Population (full-time equivalent)	615.5	42
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	46.5	49
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$2.06	36
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0=least/worst 3=most/best)	2	4

Maine

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

38

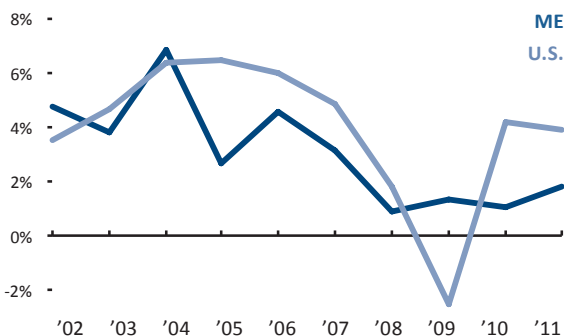
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

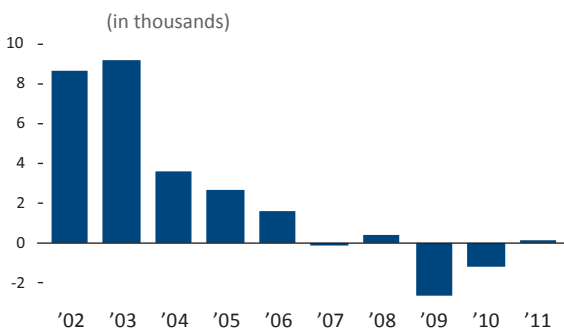
State Gross Domestic Product

Cumulative Growth 2001-2011 35.2% Rank: 46



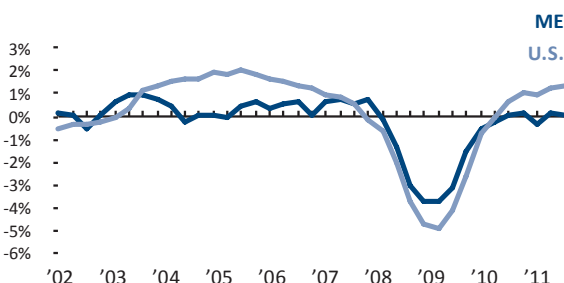
Absolute Domestic Migration

Cumulative 2002-2011 21,920 Rank: 25



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 -1.9% Rank: 38



41

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
46 47 44 48 47

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	7.95%	40
Top Marginal Corporate Income Tax Rate	8.93%	39
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$19.15	47
Property Tax Burden (per \$1,000 of personal income)	\$49.27	45
Sales Tax Burden (per \$1,000 of personal income)	\$20.55	19
Remaining Tax Burden (per \$1,000 of personal income)	\$20.70	33
Estate/Inheritance Tax Levied?	Yes	50
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$2.89	3
Debt Service as a Share of Tax Revenue	6.5%	8
Public Employees Per 10,000 of Population (full-time equivalent)	567.5	35
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	69.2	12
State Minimum Wage (federal floor is \$7.25)	\$7.50	34
Average Workers' Compensation Costs (per \$100 of payroll)	\$2.24	41
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	1	15

Maryland

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

28

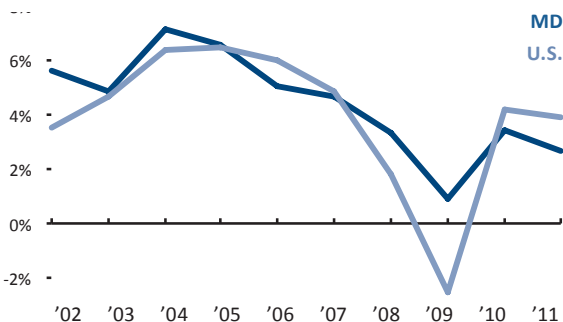
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

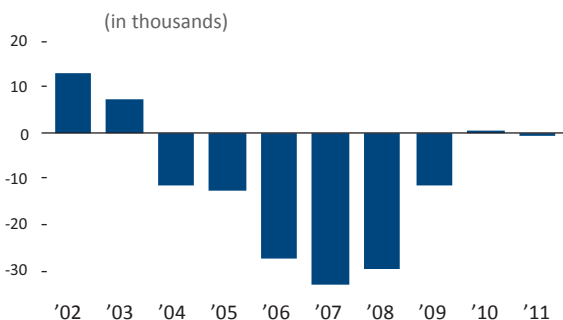
State Gross Domestic Product

Cumulative Growth 2001-2011 53.9% Rank: 18



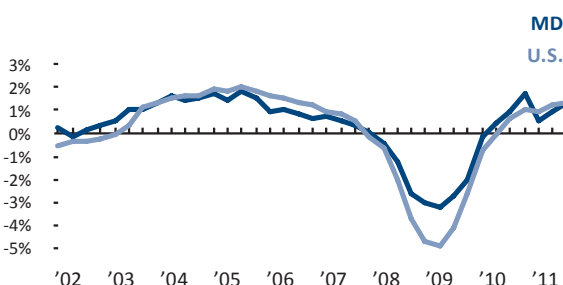
Absolute Domestic Migration

Cumulative 2002-2011 -104,391 Rank: 42



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 3.7% Rank: 16



35

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
28 28 29 21 20

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	8.95%	44
Top Marginal Corporate Income Tax Rate	8.25%	35
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$6.95	22
Property Tax Burden (per \$1,000 of personal income)	\$30.71	19
Sales Tax Burden (per \$1,000 of personal income)	\$13.65	8
Remaining Tax Burden (per \$1,000 of personal income)	\$18.08	21
Estate/Inheritance Tax Levied?	Yes	50
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$1.61	43
Debt Service as a Share of Tax Revenue	6.5%	9
Public Employees Per 10,000 of Population (full-time equivalent)	526.8	21
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	58.3	33
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.68	17
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0=least/worst 3=most/best)	0	34

Massachusetts

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

45

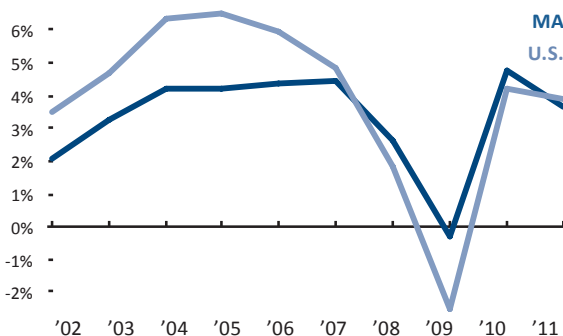
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

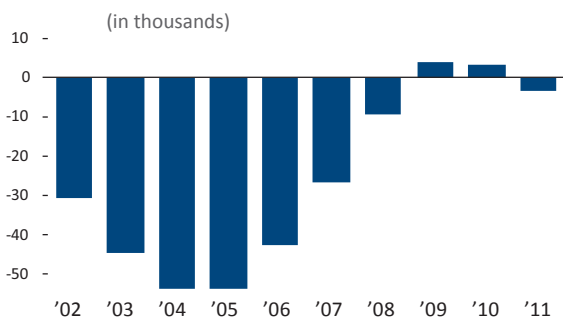
State Gross Domestic Product

Cumulative Growth 2001-2011 38.7% Rank: 40



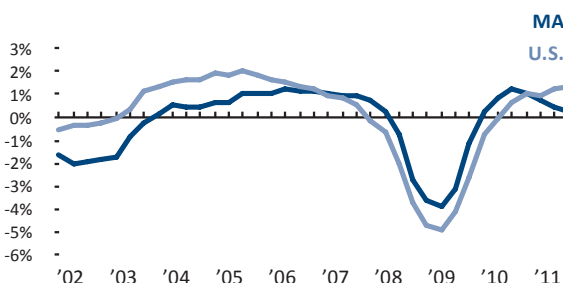
Absolute Domestic Migration

Cumulative 2002-2011 -260,153 Rank: 43



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 -2.5% Rank: 42



29

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
22 26 32 24 25

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	5.25%	21
Top Marginal Corporate Income Tax Rate	8.00%	32
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$3.08	16
Property Tax Burden (per \$1,000 of personal income)	\$39.71	36
Sales Tax Burden (per \$1,000 of personal income)	\$14.15	9
Remaining Tax Burden (per \$1,000 of personal income)	\$11.94	2
Estate/Inheritance Tax Levied?	Yes	50
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$0.69	38
Debt Service as a Share of Tax Revenue	13.3%	49
Public Employees Per 10,000 of Population (full-time equivalent)	486.9	8
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	66.3	19
State Minimum Wage (federal floor is \$7.25)	\$8.00	43
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.37	7
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0=least/worst 3=most/best)	1	15

Michigan

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX



50

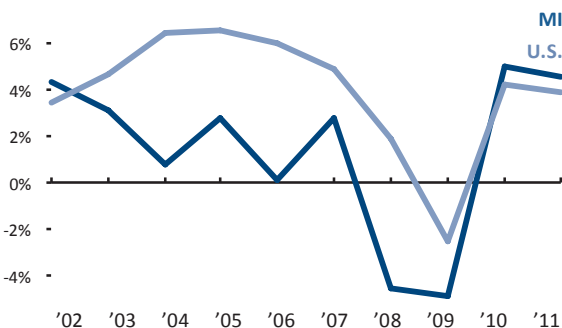
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

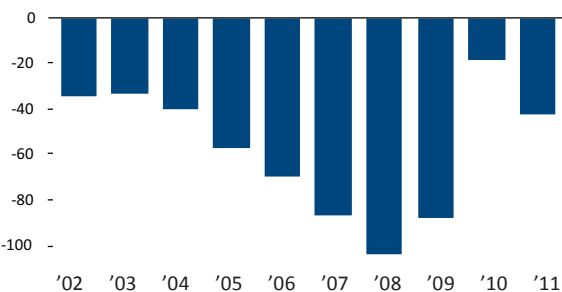
State Gross Domestic Product

Cumulative Growth 2001-2011 14.2% Rank: 50



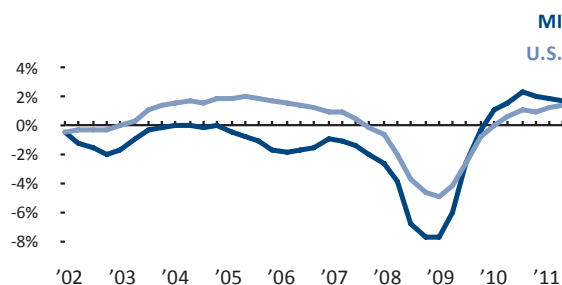
Absolute Domestic Migration

Cumulative 2002-2011 -574,013 Rank: 47
(in thousands)



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 -12.2% Rank: 50



20

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
17 34 26 25 17

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	6.65%	28
Top Marginal Corporate Income Tax Rate	8.00%	32
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$2.24	15
Property Tax Burden (per \$1,000 of personal income)	\$43.41	40
Sales Tax Burden (per \$1,000 of personal income)	\$27.96	37
Remaining Tax Burden (per \$1,000 of personal income)	\$16.47	13
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$0.99	9
Debt Service as a Share of Tax Revenue	9.1%	30
Public Employees Per 10,000 of Population (full-time equivalent)	462.3	3
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	63.0	27
State Minimum Wage (federal floor is \$7.25)	\$7.40	33
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.73	19
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0=least/worst 3=most/best)	2	4

Minnesota

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

34

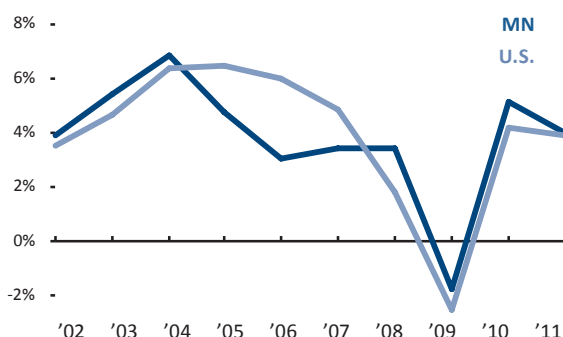
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

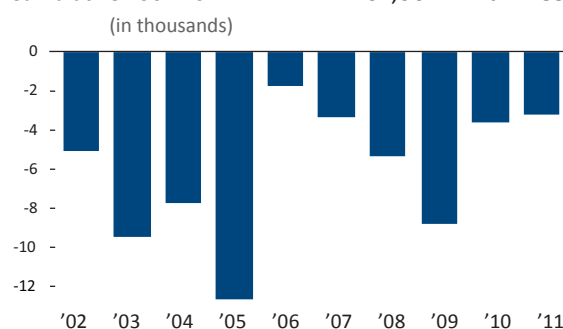
State Gross Domestic Product

Cumulative Growth 2001-2011 45.2% Rank: 29



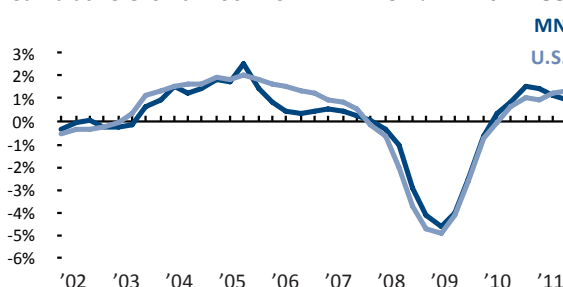
Absolute Domestic Migration

Cumulative 2002-2011 -61,061 Rank: 39



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 0.2% Rank: 33



46

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison

ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012

39 40 38 37 41

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	7.85%	39
Top Marginal Corporate Income Tax Rate	9.80%	45
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$18.12	46
Property Tax Burden (per \$1,000 of personal income)	\$34.11	25
Sales Tax Burden (per \$1,000 of personal income)	\$20.69	20
Remaining Tax Burden (per \$1,000 of personal income)	\$23.48	44
Estate/Inheritance Tax Levied?	Yes	50
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$1.58	42
Debt Service as a Share of Tax Revenue	8.2%	24
Public Employees Per 10,000 of Population (full-time equivalent)	518.6	18
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	71.4	4
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$2.03	34
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0=least/worst 3=most/best)	0	34

Mississippi

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

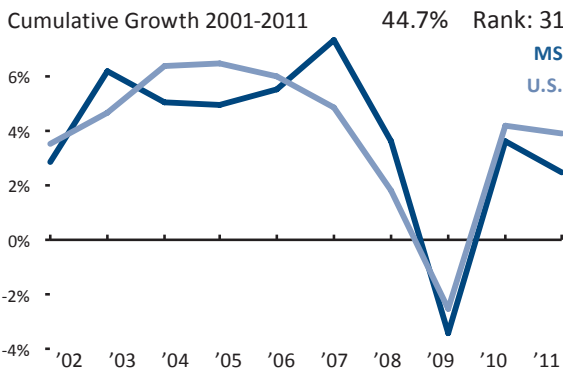
40

Economic
Performance Rank

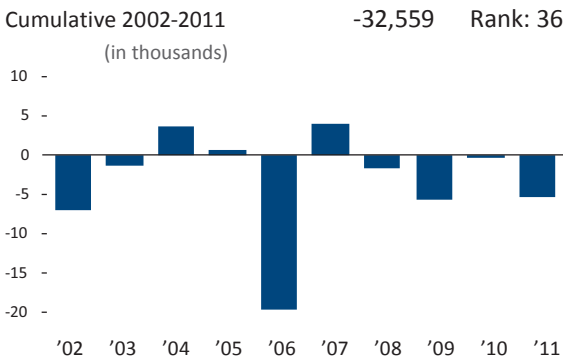
Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

State Gross Domestic Product



Absolute Domestic Migration



Non-Farm Payroll Employment



10

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
19 19 18 19 15

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	5.00%	17
Top Marginal Corporate Income Tax Rate	5.00%	8
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$7.53	24
Property Tax Burden (per \$1,000 of personal income)	\$28.22	16
Sales Tax Burden (per \$1,000 of personal income)	\$31.77	42
Remaining Tax Burden (per \$1,000 of personal income)	\$20.44	32
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$0.00	27
Debt Service as a Share of Tax Revenue	6.0%	5
Public Employees Per 10,000 of Population (full-time equivalent)	644.6	44
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	46.6	48
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.49	9
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0=least/worst 3=most/best)	2	4

Missouri

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

42

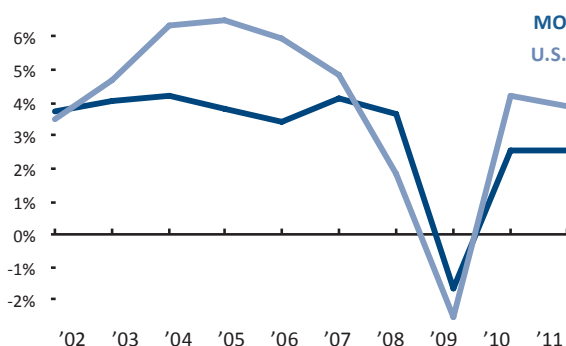
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

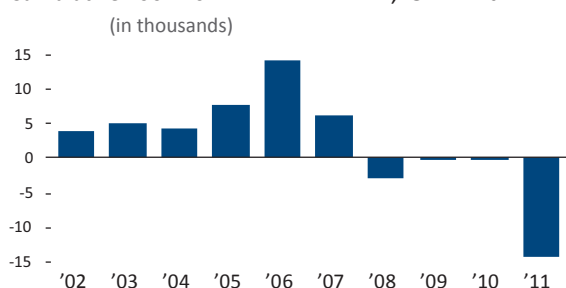
State Gross Domestic Product

Cumulative Growth 2001-2011 34.6% Rank: 47



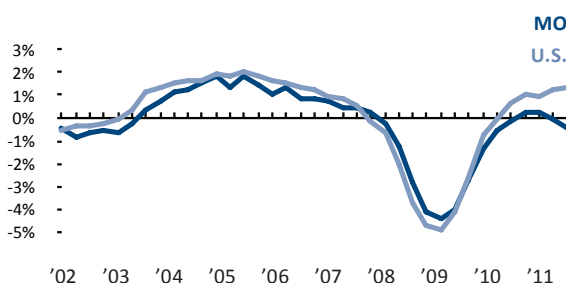
Absolute Domestic Migration

Cumulative 2002-2011 24,454 Rank: 24



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 -2.6% Rank: 43



23

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison	2008	2009	2010	2011	2012
ECONOMIC OUTLOOK RANK	25	23	15	9	7

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	7.00%	33
Top Marginal Corporate Income Tax Rate	6.16%	17
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$12.96	36
Property Tax Burden (per \$1,000 of personal income)	\$26.74	14
Sales Tax Burden (per \$1,000 of personal income)	\$22.41	22
Remaining Tax Burden (per \$1,000 of personal income)	\$16.53	14
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$0.11	22
Debt Service as a Share of Tax Revenue	9.2%	33
Public Employees Per 10,000 of Population (full-time equivalent)	527.9	22
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	57.8	34
State Minimum Wage (federal floor is \$7.25)	\$7.35	32
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.62	15
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	3	1

Montana

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

9

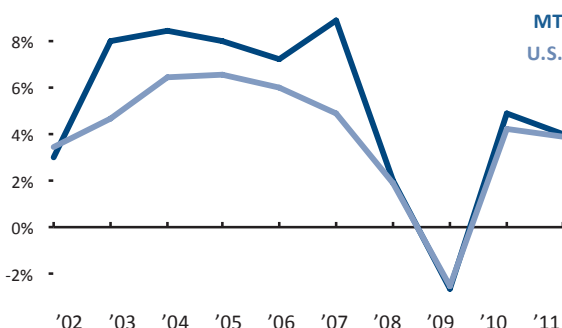
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

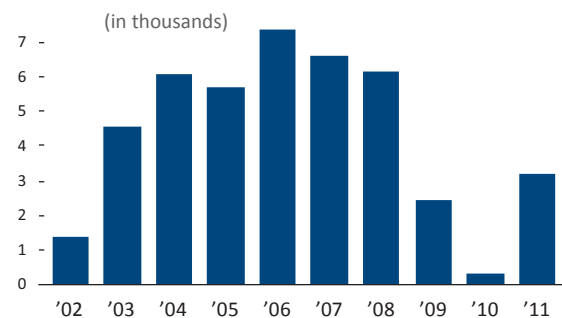
State Gross Domestic Product

Cumulative Growth 2001-2011 64.6% Rank: 9



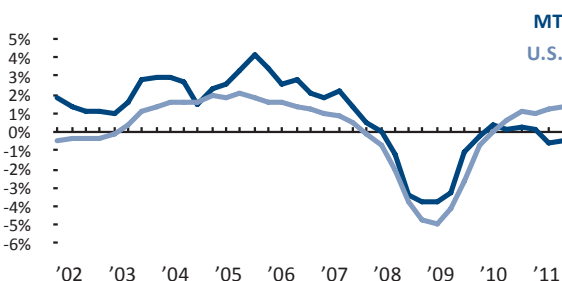
Absolute Domestic Migration

Cumulative 2002-2011 43,815 Rank: 20



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 8.7% Rank: 8



42

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
32 30 33 36 36

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	6.90%	31
Top Marginal Corporate Income Tax Rate	6.75%	21
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$17.48	45
Property Tax Burden (per \$1,000 of personal income)	\$38.46	33
Sales Tax Burden (per \$1,000 of personal income)	\$0.00	1
Remaining Tax Burden (per \$1,000 of personal income)	\$26.36	46
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$0.64	13
Debt Service as a Share of Tax Revenue	7.4%	15
Public Employees Per 10,000 of Population (full-time equivalent)	579.8	38
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	52.2	45
State Minimum Wage (federal floor is \$7.25)	\$7.80	40
Average Workers' Compensation Costs (per \$100 of payroll)	\$2.50	43
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0=least/worst 3=most/best)	0	34

Nebraska

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

21

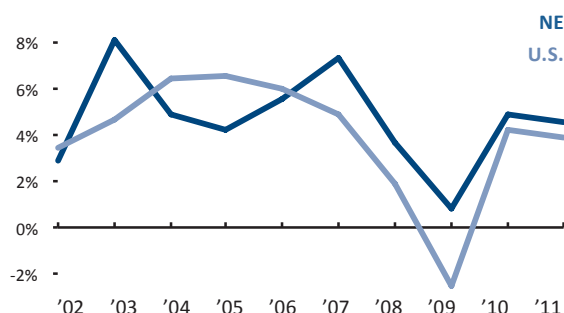
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

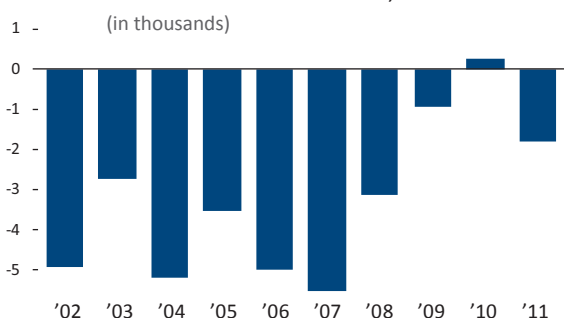
State Gross Domestic Product

Cumulative Growth 2001-2011 57.8% Rank: 14



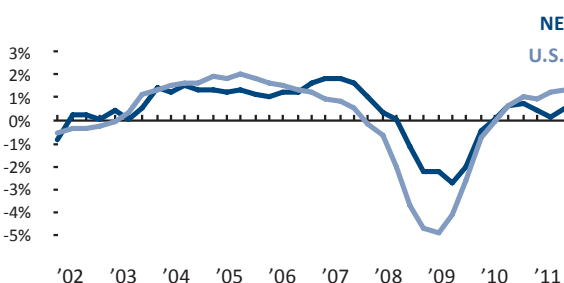
Absolute Domestic Migration

Cumulative 2002-2011 -32,456 Rank: 35



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 3.5% Rank: 17



37

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
34 29 34 32 31

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	6.84%	30
Top Marginal Corporate Income Tax Rate	7.81%	29
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$15.99	44
Property Tax Burden (per \$1,000 of personal income)	\$38.49	34
Sales Tax Burden (per \$1,000 of personal income)	\$22.73	23
Remaining Tax Burden (per \$1,000 of personal income)	\$19.72	29
Estate/Inheritance Tax Levied?	Yes	50
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$0.20	34
Debt Service as a Share of Tax Revenue	8.1%	22
Public Employees Per 10,000 of Population (full-time equivalent)	656.5	46
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	74.1	2
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.71	18
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0=least/worst 3=most/best)	0	34

Nevada

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

2

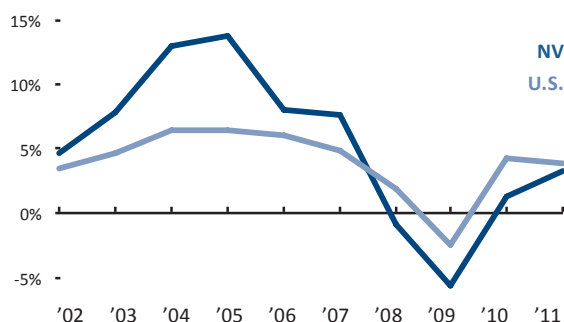
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

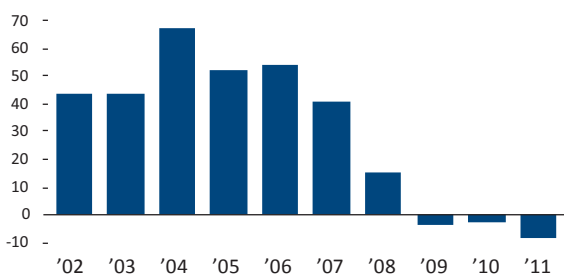
State Gross Domestic Product

Cumulative Growth 2001-2011 64.9% Rank: 8



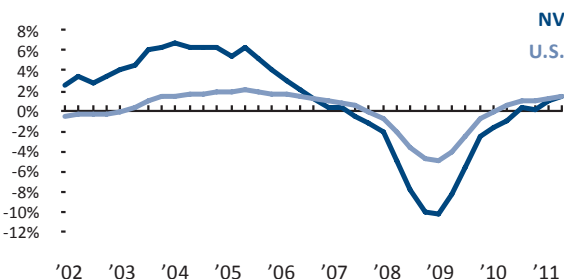
Absolute Domestic Migration

Cumulative 2002-2011 302,404 Rank: 7
(in thousands)



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 9.0% Rank: 6



13

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
7 7 11 17 18

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	0.00%	1
Top Marginal Corporate Income Tax Rate	0.00%	1
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$0.00	2
Property Tax Burden (per \$1,000 of personal income)	\$36.57	30
Sales Tax Burden (per \$1,000 of personal income)	\$29.71	40
Remaining Tax Burden (per \$1,000 of personal income)	\$37.84	49
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$6.20	48
Debt Service as a Share of Tax Revenue	10.5%	39
Public Employees Per 10,000 of Population (full-time equivalent)	419.7	1
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	57.0	37
State Minimum Wage (federal floor is \$7.25)	\$8.25	45
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.33	5
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	2	4

New Hampshire

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

32

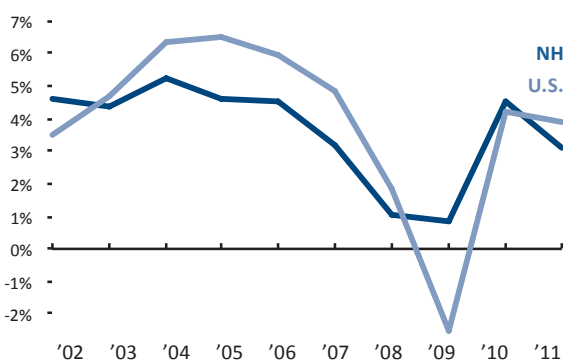
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

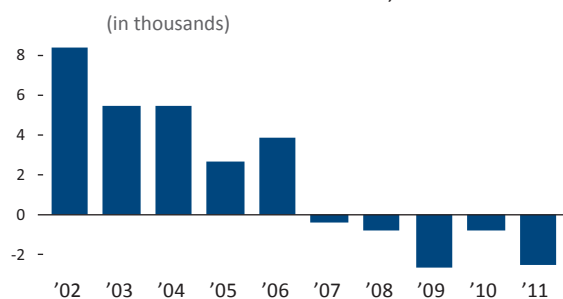
State Gross Domestic Product

Cumulative Growth 2001-2011 42.2% Rank: 35



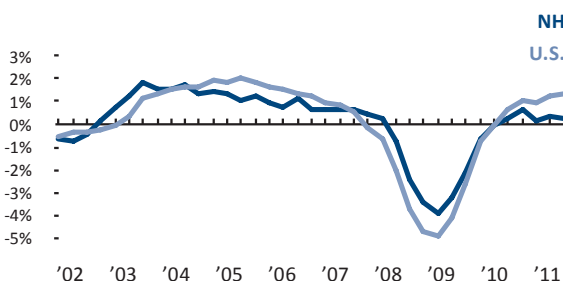
Absolute Domestic Migration

Cumulative 2002-2011 18,687 Rank: 26



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 0.9% Rank: 29



27

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
26 37 30 28 28

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	0.00%	1
Top Marginal Corporate Income Tax Rate	8.50%	36
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$0.00	2
Property Tax Burden (per \$1,000 of personal income)	\$57.24	49
Sales Tax Burden (per \$1,000 of personal income)	\$0.00	1
Remaining Tax Burden (per \$1,000 of personal income)	\$21.09	35
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$0.42	16
Debt Service as a Share of Tax Revenue	10.3%	38
Public Employees Per 10,000 of Population (full-time equivalent)	548.3	27
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	65.7	21
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$2.40	42
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	0	34

New Jersey

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

48

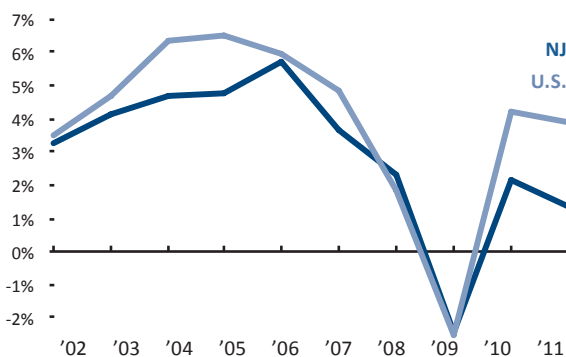
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

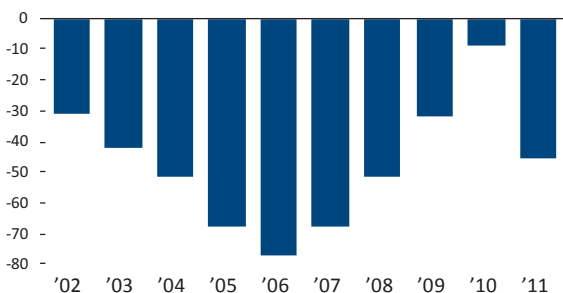
State Gross Domestic Product

Cumulative Growth 2001-2011 33.4% Rank: 48



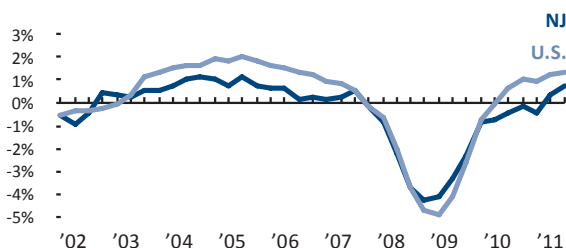
Absolute Domestic Migration

Cumulative 2002-2011 -473,234 Rank: 46
(in thousands)



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 -3.1% Rank: 46



39

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
48 46 48 45 42

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	9.97%	46
Top Marginal Corporate Income Tax Rate	9.00%	40
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$24.81	48
Property Tax Burden (per \$1,000 of personal income)	\$56.71	48
Sales Tax Burden (per \$1,000 of personal income)	\$18.10	13
Remaining Tax Burden (per \$1,000 of personal income)	\$13.95	6
Estate/Inheritance Tax Levied?	Yes	50
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$0.51	15
Debt Service as a Share of Tax Revenue	7.0%	11
Public Employees Per 10,000 of Population (full-time equivalent)	553.3	29
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	60.1	32
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$2.74	44
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	1	15

New Mexico

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

18

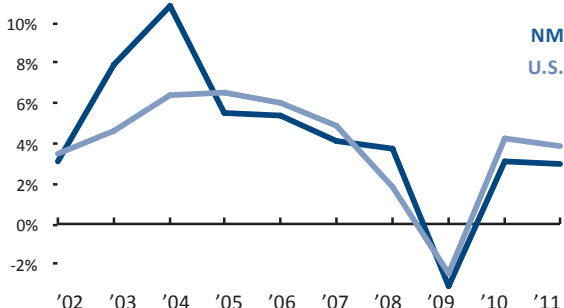
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

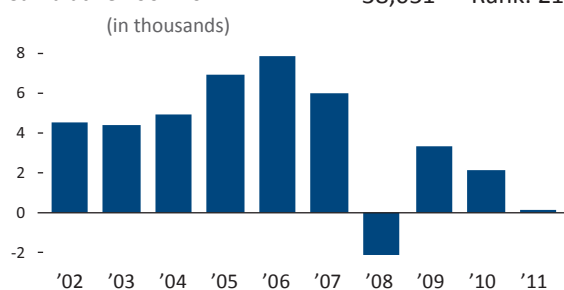
State Gross Domestic Product

Cumulative Growth 2001-2011 52.5% Rank: 20



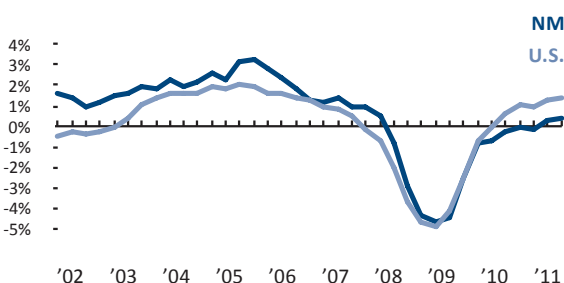
Absolute Domestic Migration

Cumulative 2002-2011 38,051 Rank: 21



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 6.2% Rank: 13



33

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
27 25 35 39 35

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	4.90%	15
Top Marginal Corporate Income Tax Rate	7.60%	28
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$10.26	28
Property Tax Burden (per \$1,000 of personal income)	\$19.53	5
Sales Tax Burden (per \$1,000 of personal income)	\$38.25	48
Remaining Tax Burden (per \$1,000 of personal income)	\$14.59	8
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$0.73	10
Debt Service as a Share of Tax Revenue	8.6%	25
Public Employees Per 10,000 of Population (full-time equivalent)	603.5	40
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	52.7	44
State Minimum Wage (federal floor is \$7.25)	\$7.50	34
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.88	24
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	0	34

New York

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX



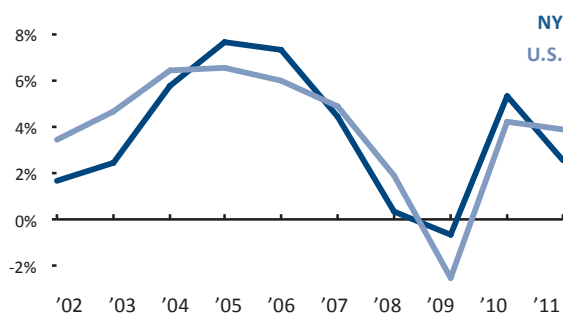
37 Economic Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

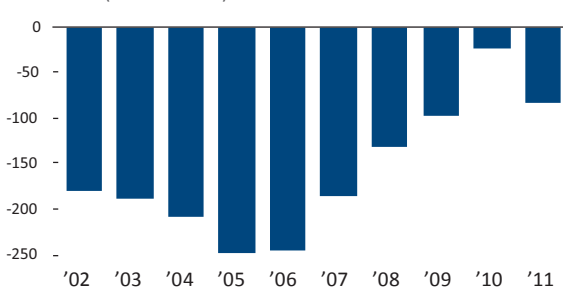
State Gross Domestic Product

Cumulative Growth 2001-2011 43.1% Rank: 33



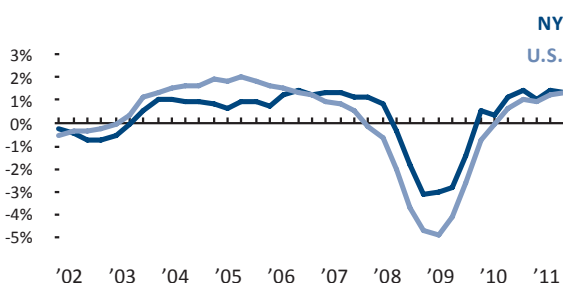
Absolute Domestic Migration

Cumulative 2002-2011 -1,591,647 Rank: 50
(in thousands)



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 2.8% Rank: 20



49 Economic Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
49 50 50 50 50

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	12.70%	49
Top Marginal Corporate Income Tax Rate	17.16%	50
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$12.15	34
Property Tax Burden (per \$1,000 of personal income)	\$47.67	44
Sales Tax Burden (per \$1,000 of personal income)	\$23.97	26
Remaining Tax Burden (per \$1,000 of personal income)	\$19.85	30
Estate/Inheritance Tax Levied?	Yes	50
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$0.09	23
Debt Service as a Share of Tax Revenue	9.5%	34
Public Employees Per 10,000 of Population (full-time equivalent)	604.0	41
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	66.4	18
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$2.82	46
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	0	34

North Carolina

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

15

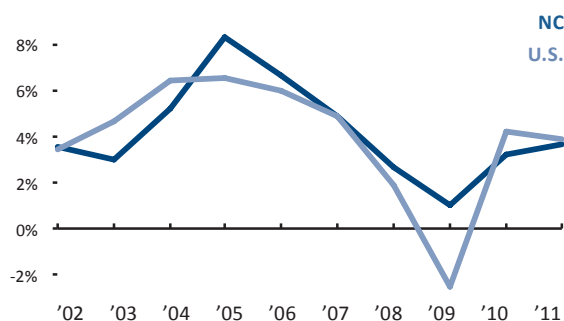
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

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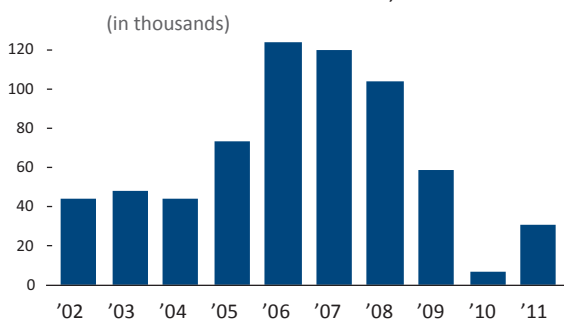
State Gross Domestic Product

Cumulative Growth 2001-2011 50.7% Rank: 23



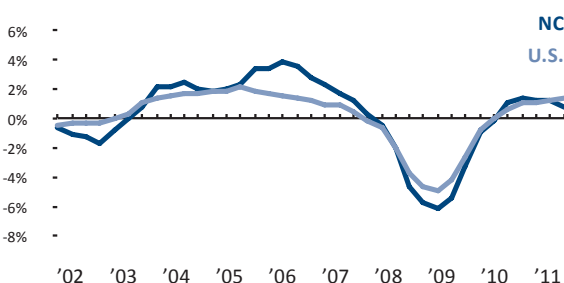
Absolute Domestic Migration

Cumulative 2002-2011 655,112 Rank: 3



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 2.1% Rank: 23



22

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison
ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
21 21 21 26 23

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	7.75%	37
Top Marginal Corporate Income Tax Rate	6.90%	22
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$11.06	31
Property Tax Burden (per \$1,000 of personal income)	\$26.35	12
Sales Tax Burden (per \$1,000 of personal income)	\$24.45	29
Remaining Tax Burden (per \$1,000 of personal income)	\$17.69	20
Estate/Inheritance Tax Levied?	Yes	50
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$2.87	4
Debt Service as a Share of Tax Revenue	7.7%	19
Public Employees Per 10,000 of Population (full-time equivalent)	575.9	36
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	65.8	20
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.90	26
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0=least/worst 3=most/best)	1	15

North Dakota

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

5

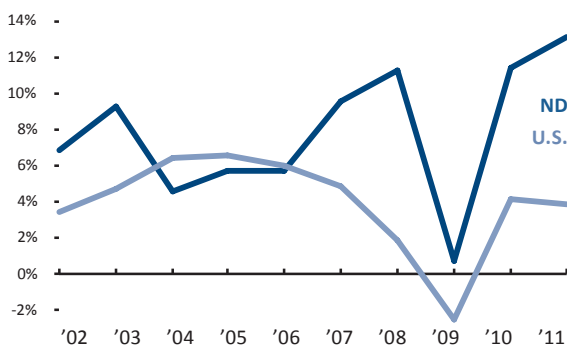
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

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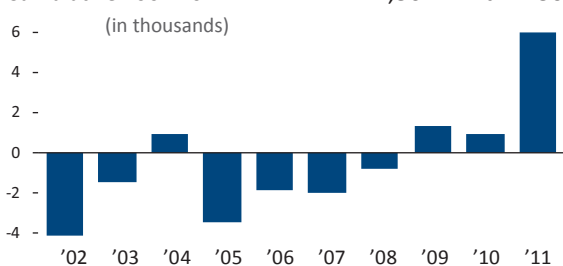
State Gross Domestic Product

Cumulative Growth 2001-2011 110.9% Rank: 1



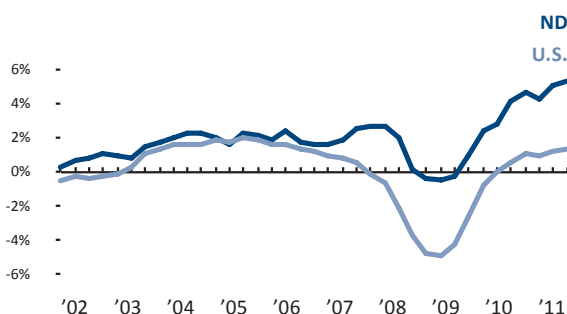
Absolute Domestic Migration

Cumulative 2002-2011 -4,367 Rank: 30



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 22.2% Rank: 1



2

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
18 13 12 7 5

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	3.99%	11
Top Marginal Corporate Income Tax Rate	5.15%	11
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$11.06	30
Property Tax Burden (per \$1,000 of personal income)	\$25.30	10
Sales Tax Burden (per \$1,000 of personal income)	\$26.29	34
Remaining Tax Burden (per \$1,000 of personal income)	\$20.10	31
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$15.48	1
Debt Service as a Share of Tax Revenue	5.8%	4
Public Employees Per 10,000 of Population (full-time equivalent)	658.6	47
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	69.8	8
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.01	1
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	0	34

Ohio

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

49

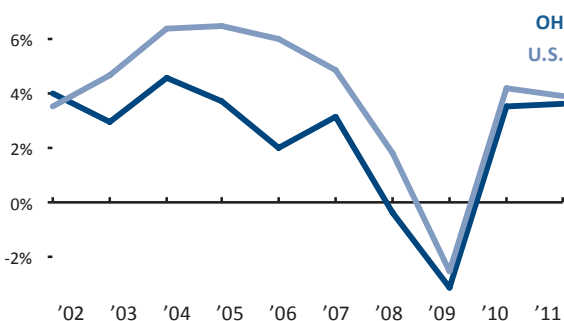
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

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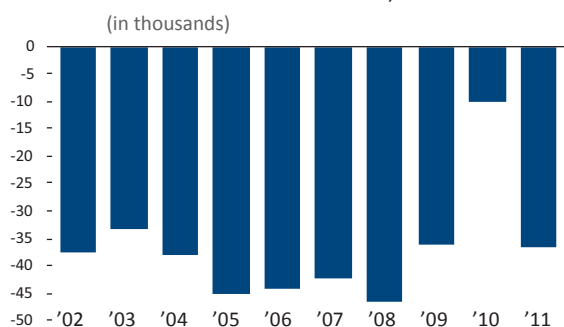
State Gross Domestic Product

Cumulative Growth 2001-2011 26.5% Rank: 49



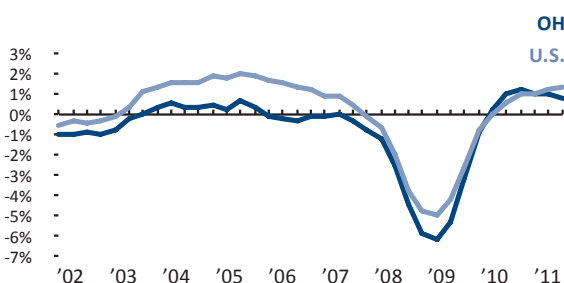
Absolute Domestic Migration

Cumulative 2002-2011 -370,201 Rank: 45



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 -7.1% Rank: 49



26

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
47 45 42 38 37

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	8.43%	43
Top Marginal Corporate Income Tax Rate	3.65%	5
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$14.12	38
Property Tax Burden (per \$1,000 of personal income)	\$32.11	21
Sales Tax Burden (per \$1,000 of personal income)	\$18.77	15
Remaining Tax Burden (per \$1,000 of personal income)	\$22.52	39
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$0.70	11
Debt Service as a Share of Tax Revenue	7.7%	18
Public Employees Per 10,000 of Population (full-time equivalent)	515.1	16
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	62.1	30
State Minimum Wage (federal floor is \$7.25)	\$7.85	42
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.84	23
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0=least/worst 3=most/best)	1	15

Oklahoma

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

12

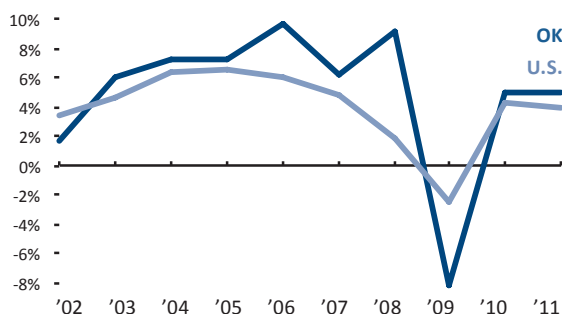
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

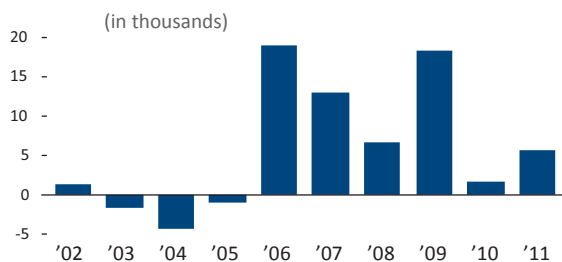
State Gross Domestic Product

Cumulative Growth 2001-2011 59.6% Rank: 10



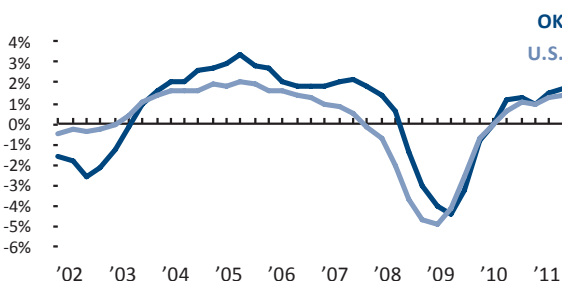
Absolute Domestic Migration

Cumulative 2002-2011 58,791 Rank: 18



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 5.2% Rank: 15



19

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
14 15 14 14 14

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	5.25%	21
Top Marginal Corporate Income Tax Rate	6.00%	14
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$7.67	26
Property Tax Burden (per \$1,000 of personal income)	\$18.72	2
Sales Tax Burden (per \$1,000 of personal income)	\$28.09	38
Remaining Tax Burden (per \$1,000 of personal income)	\$17.27	19
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$1.02	40
Debt Service as a Share of Tax Revenue	7.2%	13
Public Employees Per 10,000 of Population (full-time equivalent)	566.4	34
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	55.0	42
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$2.77	45
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0=least/worst 3=most/best)	2	4

Oregon

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

11

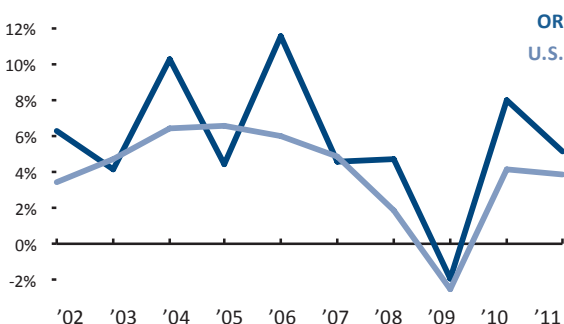
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

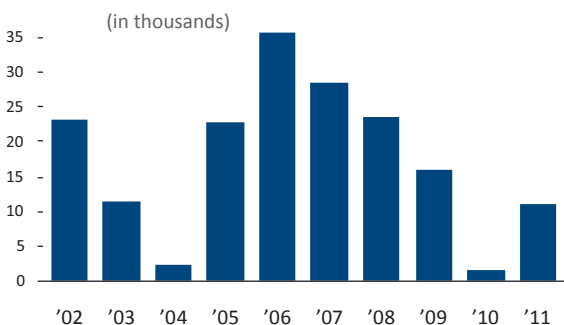
State Gross Domestic Product

Cumulative Growth 2001-2011 73.1% Rank: 5



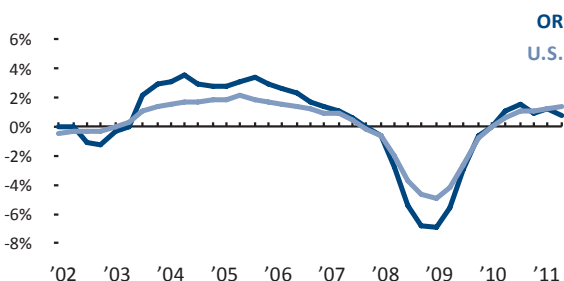
Absolute Domestic Migration

Cumulative 2002-2011 176,391 Rank: 11



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 2.1% Rank: 22



44

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
35 39 41 43 45

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	10.61%	47
Top Marginal Corporate Income Tax Rate	11.25%	48
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$15.01	40
Property Tax Burden (per \$1,000 of personal income)	\$36.65	31
Sales Tax Burden (per \$1,000 of personal income)	\$0.00	1
Remaining Tax Burden (per \$1,000 of personal income)	\$20.97	34
Estate/Inheritance Tax Levied?	Yes	50
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$3.07	46
Debt Service as a Share of Tax Revenue	9.5%	35
Public Employees Per 10,000 of Population (full-time equivalent)	509.6	14
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	62.6	28
State Minimum Wage (federal floor is \$7.25)	\$8.95	49
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.58	12
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0=least/worst 3=most/best)	2	4

Pennsylvania

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

33

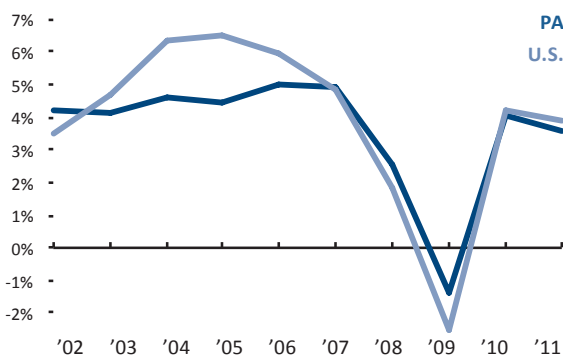
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

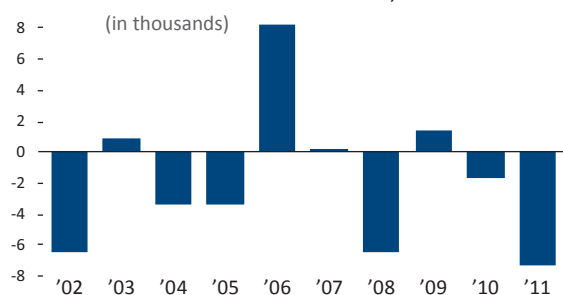
State Gross Domestic Product

Cumulative Growth 2001-2011 42.3% Rank: 34



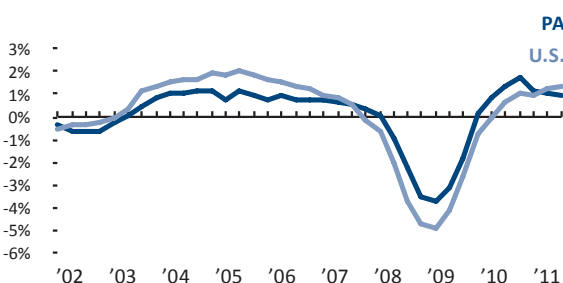
Absolute Domestic Migration

Cumulative 2002-2011 -17,743 Rank: 31



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 1.0% Rank: 27



34

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
36 42 43 41 40

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	7.00%	32
Top Marginal Corporate Income Tax Rate	17.07%	49
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$0.00	2
Property Tax Burden (per \$1,000 of personal income)	\$31.86	20
Sales Tax Burden (per \$1,000 of personal income)	\$17.15	12
Remaining Tax Burden (per \$1,000 of personal income)	\$25.45	45
Estate/Inheritance Tax Levied?	Yes	50
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$2.93	2
Debt Service as a Share of Tax Revenue	8.9%	28
Public Employees Per 10,000 of Population (full-time equivalent)	464.5	4
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	56.3	39
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$2.15	39
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0=least/worst 3=most/best)	0	34

Rhode Island

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

44

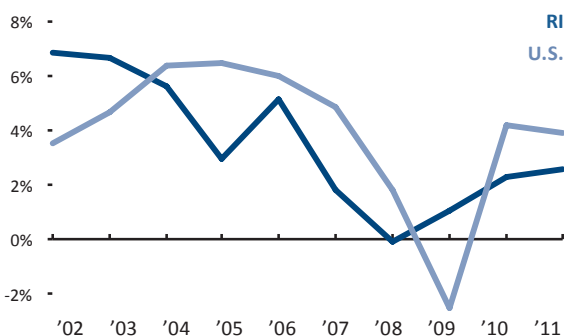
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

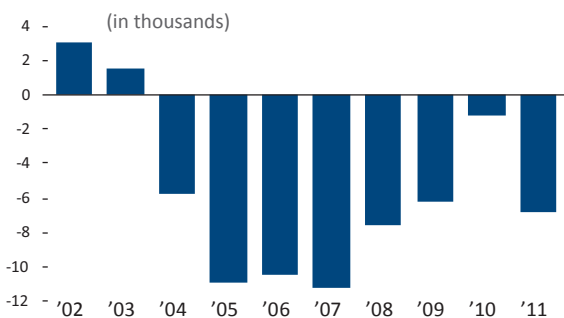
State Gross Domestic Product

Cumulative Growth 2001-2011 40.3% Rank: 37



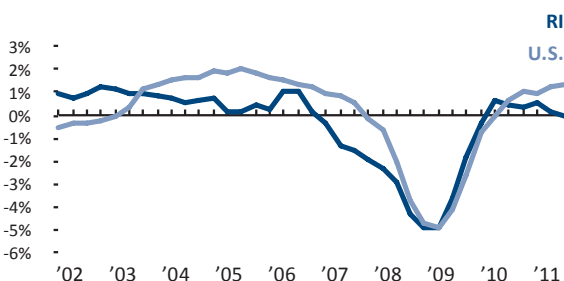
Absolute Domestic Migration

Cumulative 2002-2011 -55,255 Rank: 38



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 -3.7% Rank: 47



45

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
45 48 45 42 43

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	5.99%	25
Top Marginal Corporate Income Tax Rate	9.00%	40
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$11.53	32
Property Tax Burden (per \$1,000 of personal income)	\$50.76	46
Sales Tax Burden (per \$1,000 of personal income)	\$18.48	14
Remaining Tax Burden (per \$1,000 of personal income)	\$18.24	23
Estate/Inheritance Tax Levied?	Yes	50
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$3.64	47
Debt Service as a Share of Tax Revenue	11.5%	42
Public Employees Per 10,000 of Population (full-time equivalent)	473.2	7
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	60.9	31
State Minimum Wage (federal floor is \$7.25)	\$7.75	36
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.99	31
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0=least/worst 3=most/best)	1	15

South Carolina

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

24

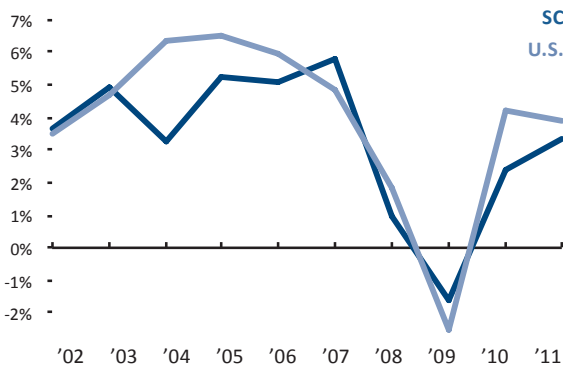
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

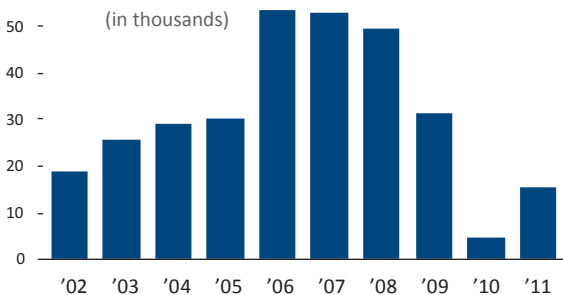
State Gross Domestic Product

Cumulative Growth 2001-2011 38.1% Rank: 41



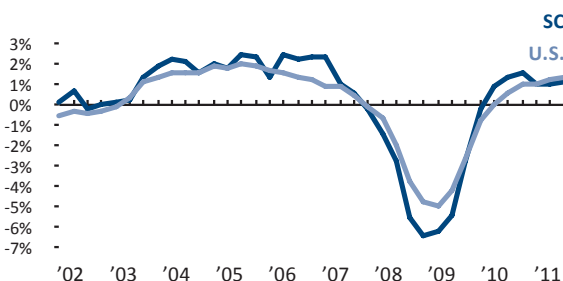
Absolute Domestic Migration

Cumulative 2002-2011 312,448 Rank: 6



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 1.7% Rank: 25



31

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
20 20 31 22 27

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	7.00%	34
Top Marginal Corporate Income Tax Rate	5.00%	8
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$15.68	42
Property Tax Burden (per \$1,000 of personal income)	\$32.28	23
Sales Tax Burden (per \$1,000 of personal income)	\$21.56	21
Remaining Tax Burden (per \$1,000 of personal income)	\$16.91	16
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$0.00	27
Debt Service as a Share of Tax Revenue	12.3%	47
Public Employees Per 10,000 of Population (full-time equivalent)	541.9	25
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	56.3	39
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$2.04	35
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	1	15

South Dakota

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX



16

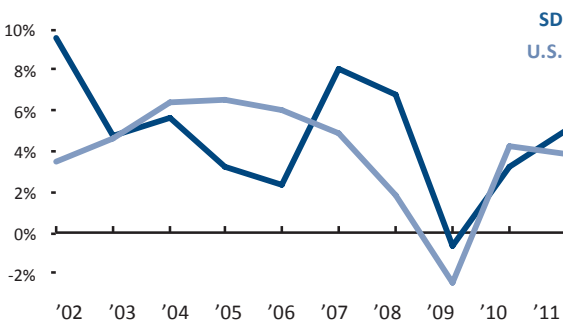
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

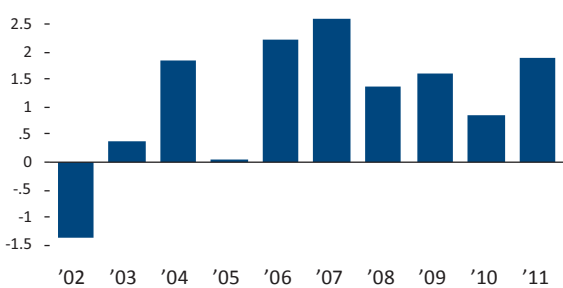
State Gross Domestic Product

Cumulative Growth 2001-2011 59.1% Rank: 12



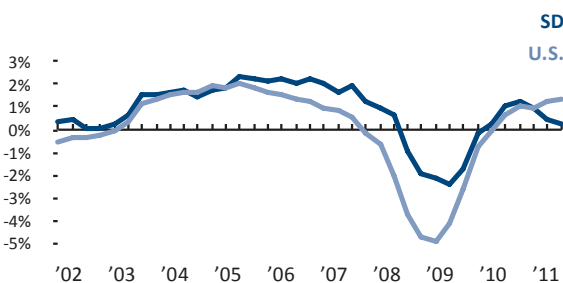
Absolute Domestic Migration

Cumulative 2002-2011 11,502 Rank: 27
(in thousands)



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 7.7% Rank: 10



3

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison	2008	2009	2010	2011	2012
ECONOMIC OUTLOOK RANK	2	5	4	2	2

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	0.00%	1
Top Marginal Corporate Income Tax Rate	0.00%	1
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$0.00	2
Property Tax Burden (per \$1,000 of personal income)	\$29.65	17
Sales Tax Burden (per \$1,000 of personal income)	\$32.78	43
Remaining Tax Burden (per \$1,000 of personal income)	\$18.96	27
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$0.00	27
Debt Service as a Share of Tax Revenue	8.0%	21
Public Employees Per 10,000 of Population (full-time equivalent)	556.4	30
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	69.5	10
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.91	28
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0=least/worst 3=most/best)	1	15

Tennessee

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

23

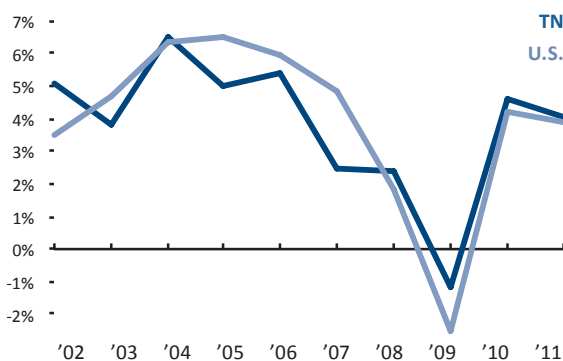
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

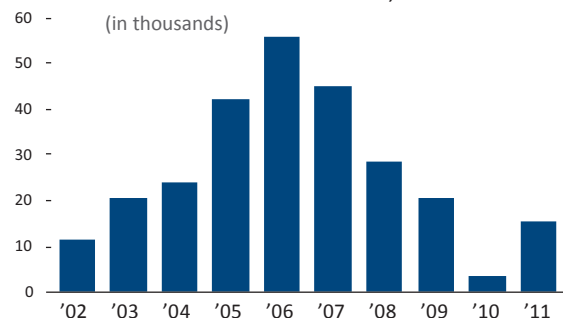
State Gross Domestic Product

Cumulative Growth 2001-2011 45.1% Rank: 30



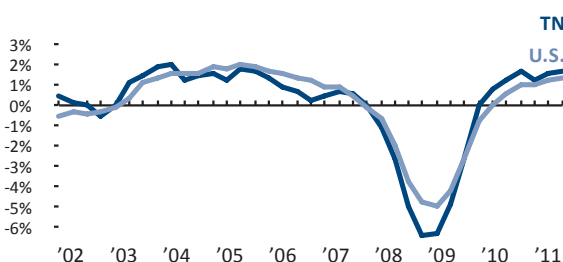
Absolute Domestic Migration

Cumulative 2002-2011 266,973 Rank: 8



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 0.5% Rank: 31



18

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison	2008	2009	2010	2011	2012
ECONOMIC OUTLOOK RANK	3	9	10	8	12

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	0.00%	1
Top Marginal Corporate Income Tax Rate	6.50%	19
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$0.00	2
Property Tax Burden (per \$1,000 of personal income)	\$23.23	8
Sales Tax Burden (per \$1,000 of personal income)	\$37.08	45
Remaining Tax Burden (per \$1,000 of personal income)	\$18.93	26
Estate/Inheritance Tax Levied?	Yes	50
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$1.72	44
Debt Service as a Share of Tax Revenue	9.2%	31
Public Employees Per 10,000 of Population (full-time equivalent)	511.4	15
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	63.7	26
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$2.02	32
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	1	15

Texas

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX



1

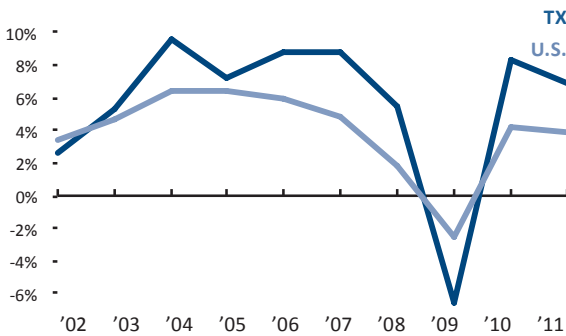
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

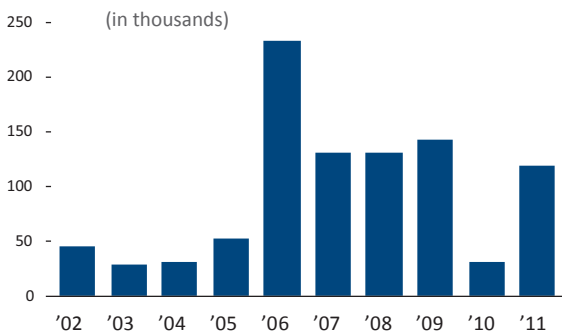
State Gross Domestic Product

Cumulative Growth 2001-2011 71.5% Rank: 7



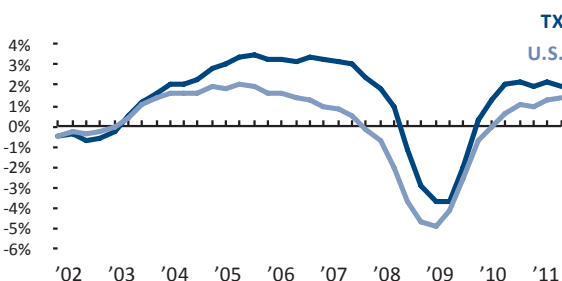
Absolute Domestic Migration

Cumulative 2002-2011 947,075 Rank: 2



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 12.4% Rank: 5



12

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
13 10 19 18 16

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	0.00%	1
Top Marginal Corporate Income Tax Rate	2.72%	4
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$0.00	2
Property Tax Burden (per \$1,000 of personal income)	\$42.26	38
Sales Tax Burden (per \$1,000 of personal income)	\$22.95	24
Remaining Tax Burden (per \$1,000 of personal income)	\$22.25	37
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$0.03	30
Debt Service as a Share of Tax Revenue	11.9%	46
Public Employees Per 10,000 of Population (full-time equivalent)	564.8	32
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	57.2	35
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.60	13
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	1	15

Utah

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

3

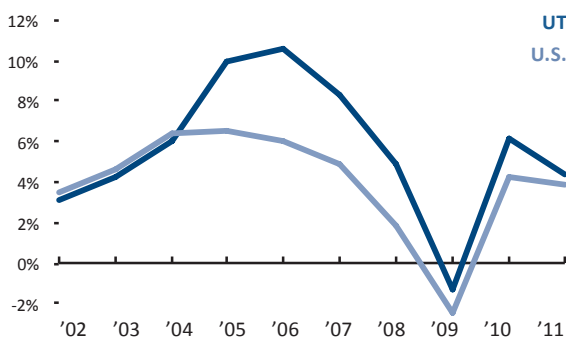
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

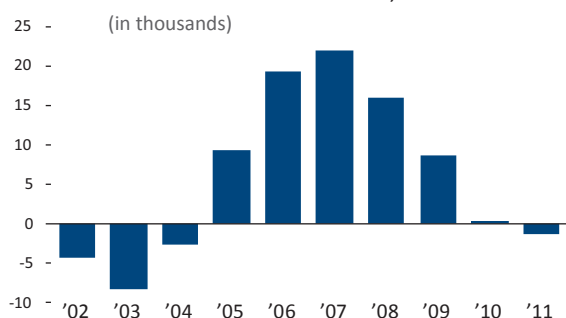
State Gross Domestic Product

Cumulative Growth 2001-2011 72.0% Rank: 6



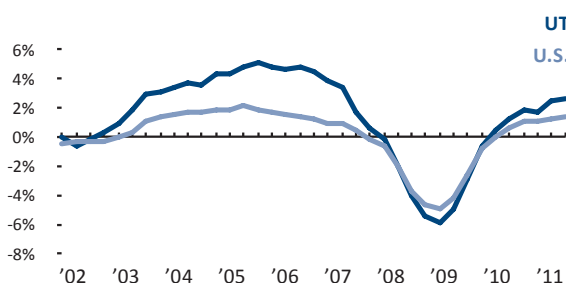
Absolute Domestic Migration

Cumulative 2002-2011 59,009 Rank: 17



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 13.6% Rank: 3



1

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison 2008 2009 2010 2011 2012
ECONOMIC OUTLOOK RANK 1 1 1 1 1

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	5.00%	17
Top Marginal Corporate Income Tax Rate	5.00%	8
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$0.00	2
Property Tax Burden (per \$1,000 of personal income)	\$26.43	13
Sales Tax Burden (per \$1,000 of personal income)	\$25.38	31
Remaining Tax Burden (per \$1,000 of personal income)	\$15.77	11
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$0.08	24
Debt Service as a Share of Tax Revenue	7.9%	20
Public Employees Per 10,000 of Population (full-time equivalent)	523.9	20
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	69.7	9
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.35	6
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	1	15

Vermont

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

36

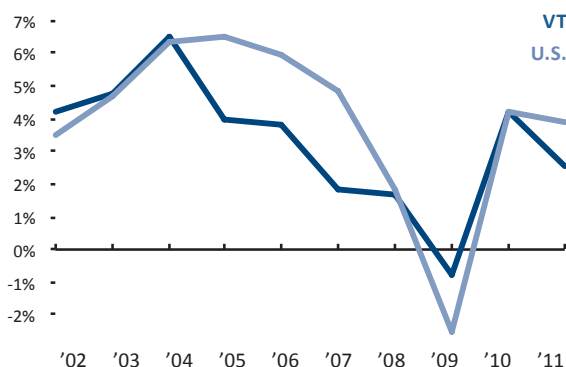
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

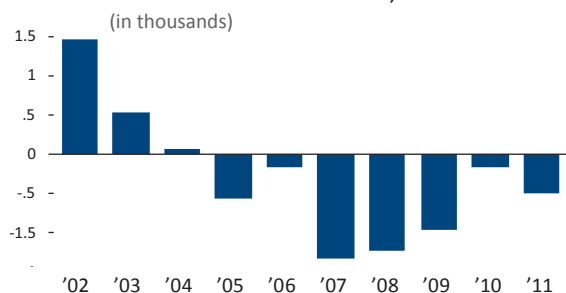
State Gross Domestic Product

Cumulative Growth 2001-2011 37.7% Rank: 43



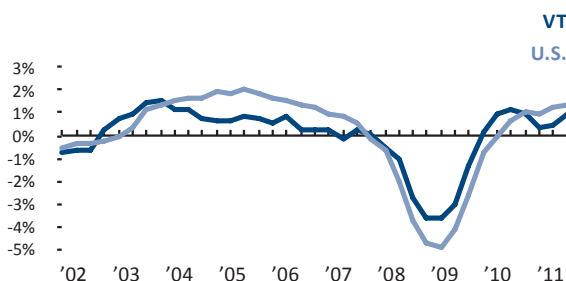
Absolute Domestic Migration

Cumulative 2002-2011 -2,848 Rank: 28



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 0.3% Rank: 32



50

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison	2008	2009	2010	2011	2012
ECONOMIC OUTLOOK RANK	50	49	49	49	49

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	8.95%	44
Top Marginal Corporate Income Tax Rate	8.50%	36
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$28.01	49
Property Tax Burden (per \$1,000 of personal income)	\$55.50	47
Sales Tax Burden (per \$1,000 of personal income)	\$13.14	6
Remaining Tax Burden (per \$1,000 of personal income)	\$28.87	48
Estate/Inheritance Tax Levied?	Yes	50
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$0.69	37
Debt Service as a Share of Tax Revenue	6.9%	10
Public Employees Per 10,000 of Population (full-time equivalent)	632.9	43
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	67.1	16
State Minimum Wage (federal floor is \$7.25)	\$8.60	48
Average Workers' Compensation Costs (per \$100 of payroll)	\$2.07	37
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	0	34

Virginia

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

13

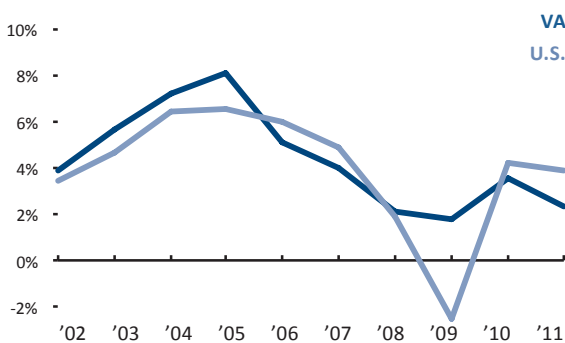
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

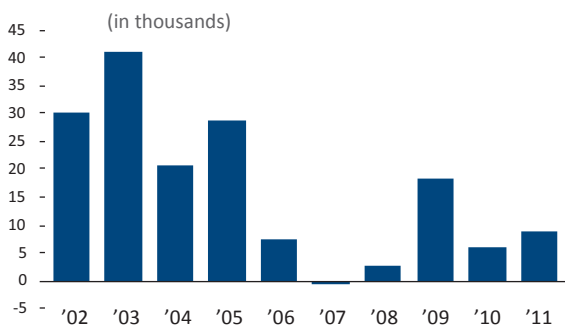
State Gross Domestic Product

Cumulative Growth 2001-2011 53.1% Rank: 19



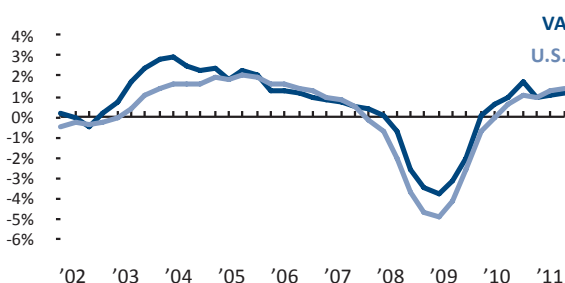
Absolute Domestic Migration

Cumulative 2002-2011 163,384 Rank: 12



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 6.0% Rank: 14



5

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
5 4 8 3 3

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	5.75%	24
Top Marginal Corporate Income Tax Rate	7.60%	27
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$6.45	20
Property Tax Burden (per \$1,000 of personal income)	\$32.57	24
Sales Tax Burden (per \$1,000 of personal income)	\$13.23	7
Remaining Tax Burden (per \$1,000 of personal income)	\$16.98	17
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$0.03	25
Debt Service as a Share of Tax Revenue	8.1%	23
Public Employees Per 10,000 of Population (full-time equivalent)	542.0	26
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	70.2	7
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.20	4
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	0	34

Washington

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

10

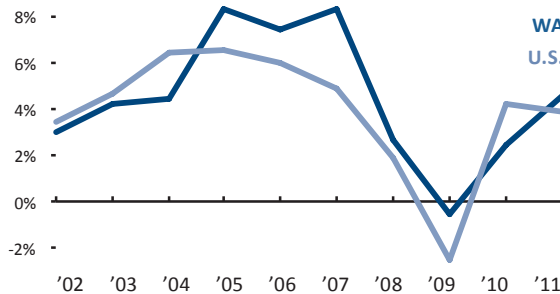
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

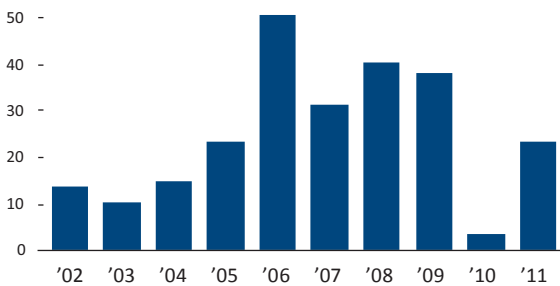
State Gross Domestic Product

Cumulative Growth 2001-2011 54.2% Rank: 17



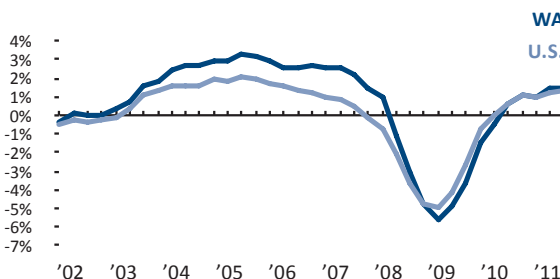
Absolute Domestic Migration

Cumulative 2002-2011 249,302 Rank: 9
(in thousands)



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 6.3% Rank: 12



36

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison
ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
30 22 24 33 33

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	0.00%	1
Top Marginal Corporate Income Tax Rate	8.00%	31
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$0.00	2
Property Tax Burden (per \$1,000 of personal income)	\$30.29	18
Sales Tax Burden (per \$1,000 of personal income)	\$33.41	44
Remaining Tax Burden (per \$1,000 of personal income)	\$23.20	42
Estate/Inheritance Tax Levied?	Yes	50
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	\$0.10	31
Debt Service as a Share of Tax Revenue	11.4%	40
Public Employees Per 10,000 of Population (full-time equivalent)	507.1	13
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	65.4	22
State Minimum Wage (federal floor is \$7.25)	\$9.19	50
Average Workers' Compensation Costs (per \$100 of payroll)	\$2.11	38
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	3	1

West Virginia

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX



19

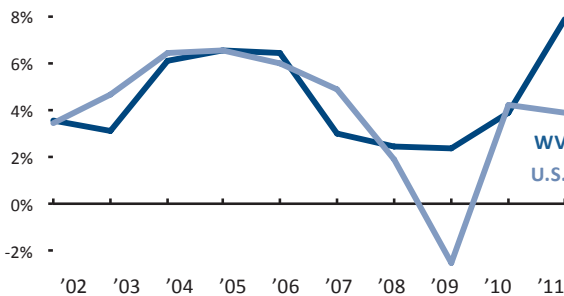
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

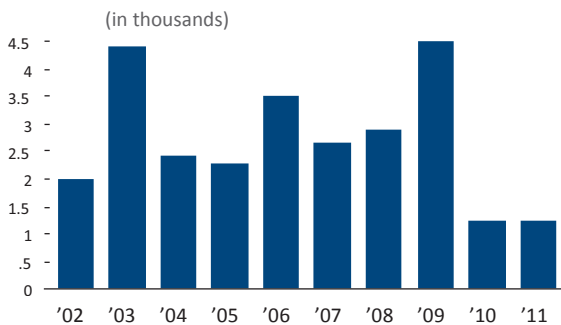
State Gross Domestic Product

Cumulative Growth 2001-2011 55.4% Rank: 16



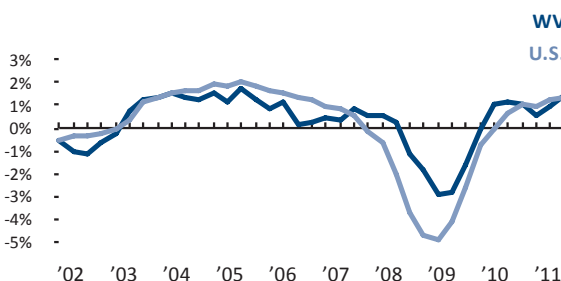
Absolute Domestic Migration

Cumulative 2002-2011 27,204 Rank: 22



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 3.4% Rank: 18



32

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
38 33 27 31 30

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	6.50%	27
Top Marginal Corporate Income Tax Rate	7.00%	24
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$15.53	41
Property Tax Burden (per \$1,000 of personal income)	\$23.90	9
Sales Tax Burden (per \$1,000 of personal income)	\$20.04	17
Remaining Tax Burden (per \$1,000 of personal income)	\$28.24	47
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$0.64	12
Debt Service as a Share of Tax Revenue	6.1%	6
Public Employees Per 10,000 of Population (full-time equivalent)	558.9	31
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	44.8	50
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.55	11
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0=least/worst 3=most/best)	0	34

Wisconsin

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

41

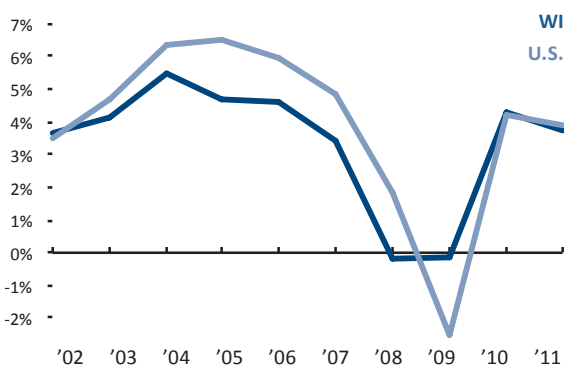
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

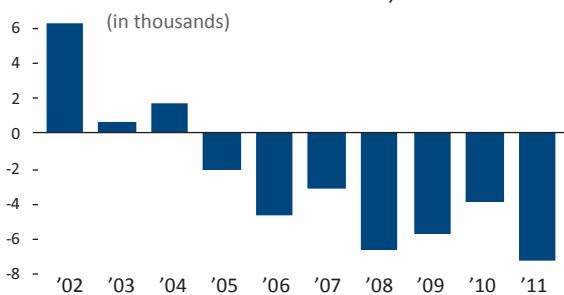
State Gross Domestic Product

Cumulative Growth 2001-2011 38.8% Rank: 39



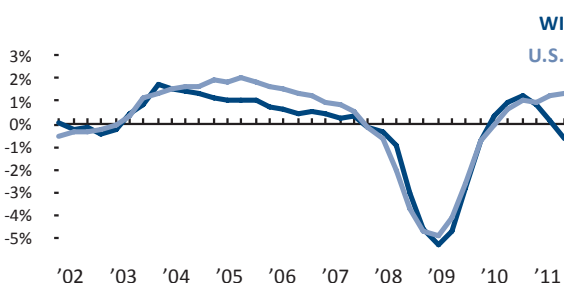
Absolute Domestic Migration

Cumulative 2002-2011 -24,370 Rank: 33



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 -2.3% Rank: 40



15

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison 2008 2009 2010 2011 2012
ECONOMIC OUTLOOK RANK 33 27 23 30 32

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	7.75%	37
Top Marginal Corporate Income Tax Rate	7.90%	30
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$3.83	17
Property Tax Burden (per \$1,000 of personal income)	\$45.60	42
Sales Tax Burden (per \$1,000 of personal income)	\$20.04	16
Remaining Tax Burden (per \$1,000 of personal income)	\$18.26	24
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$0.61	14
Debt Service as a Share of Tax Revenue	7.4%	16
Public Employees Per 10,000 of Population (full-time equivalent)	496.5	11
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	68.4	15
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$2.15	39
Right-to-Work State? (option to join or support a union)	No	50
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	2	4

Wyoming

2013 ALEC-LAFFER STATE ECONOMIC COMPETITIVENESS INDEX

4

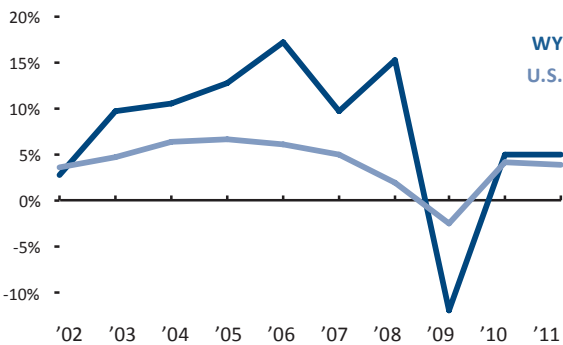
Economic
Performance Rank

Economic Performance Rank (1=best 50=worst)

A backward-looking measure based on the state's performance (equal-weighted average) in the three important performance variables shown below. These variables are highly influenced by state policy.

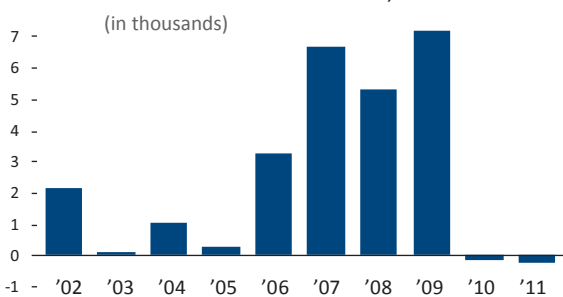
State Gross Domestic Product

Cumulative Growth 2001-2011 100.7% Rank: 2



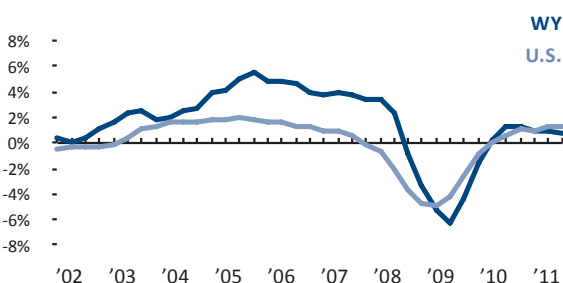
Absolute Domestic Migration

Cumulative 2002-2011 25,679 Rank: 23



Non-Farm Payroll Employment

Cumulative Growth 2001-2011 16.0% Rank: 2



4

Economic
Outlook Rank

Economic Outlook Rank (1=best 50=worst)

A forward-looking forecast based on the state's standing (equal-weighted average) in the 15 important state policy variables shown below. Data reflect state and local rates and revenues and any effect of federal deductibility.

Historical Ranking Comparison ECONOMIC OUTLOOK RANK

2008 2009 2010 2011 2012
4 6 6 4 4

Variable	Data	Rank
Top Marginal Personal Income Tax Rate	0.00%	1
Top Marginal Corporate Income Tax Rate	0.00%	1
Personal Income Tax Progressivity (change in tax liability per \$1,000 of income)	\$0.00	2
Property Tax Burden (per \$1,000 of personal income)	\$61.05	50
Sales Tax Burden (per \$1,000 of personal income)	\$39.86	49
Remaining Tax Burden (per \$1,000 of personal income)	\$12.88	3
Estate/Inheritance Tax Levied?	No	1
Recently Legislated Tax Changes (2010 & 2011, per \$1,000 of personal income)	-\$0.38	17
Debt Service as a Share of Tax Revenue	2.8%	1
Public Employees Per 10,000 of Population (full-time equivalent)	928.1	50
State Liability System Survey (tort litigation treatment, judicial impartiality, etc.)	72.6	3
State Minimum Wage (federal floor is \$7.25)	\$7.25	1
Average Workers' Compensation Costs (per \$100 of payroll)	\$1.74	20
Right-to-Work State? (option to join or support a union)	Yes	1
Number of Tax Expenditure Limits (0= least/worst 3=most/best)	0	34

Appendix

2013 ALEC-Laffer State Economic Competitiveness Index: Economic Outlook Methodology

Earlier in this book, we introduced 15 policy variables that have a proven impact on the migration of capital—both investment and human—into and out of states. The end result of an equally weighted combination of these variables is the 2013 ALEC-Laffer Economic Outlook rankings of the states. Each of these factors is influenced directly by state lawmakers through the legislative process. The 15 factors and a basic description of their purposes, sourcing, and subsequent calculation methodologies are as follows:

HIGHEST MARGINAL PERSONAL INCOME TAX RATE

This ranking includes local taxes, if any, and any impact of federal deductibility, if allowed. A state's largest city was used as a proxy for local tax rates. Data was drawn from: CCH Tax Research Network, Tax Analysts, Tax Administrators, and individual state tax return forms. Tax rates are as of January 1, 2013.

HIGHEST MARGINAL CORPORATE INCOME TAX RATE

This variable includes local taxes, if any, and includes the effect of federal deductibility, if allowed. A state's largest city was used as a proxy for local tax rates. In the case of gross receipts or business franchise taxes, an effective tax rate was approximated using NIPA profits, rental and proprietor's income, and gross domestic product data. The Texas Franchise tax is not a traditional gross receipts tax, but is instead a "margin" tax with more than one rate. A margin tax creates less distortion than does a gross receipts tax. Therefore, what we believe is the best measurement for an effective corporate tax rate for Texas is to average the 4.4 percent measure we would use if the tax was a gross receipts tax and the 1 percent highest rate on its margin tax, leading to our measure of 2.7 percent. Data was drawn from: CCH Tax Research Network, Tax Analysts, Tax Administrators, individual state tax return forms, and the Bureau of Economic Analysis. Tax rates are as of January 1, 2013.

PERSONAL INCOME TAX PROGRESSIVITY

This variable was measured as the difference between the average tax liability per \$1,000 at incomes of \$50,000 and \$150,000. The tax liabilities

were measured using a combination of effective tax rates, exemptions, and deductions at both state and federal levels, which are calculations from Laffer Associates.

PROPERTY TAX BURDEN

This variable was calculated by taking tax revenues from property taxes per \$1,000 of personal income. We have used U.S. Census Bureau data, for which the most recent year available is 2010. This data was released in September 2012.

SALES TAX BURDEN

This variable was calculated by taking tax revenues from sales taxes per \$1,000 of personal income. Sales taxes taken into consideration include the general sales tax and specific sales taxes. We have used U.S. Census Bureau Data, for which the most recent year available is 2010. Where appropriate, gross receipts or business franchise taxes, counted as sales taxes in the Census data, were subtracted from a state's total sales taxes in order to avoid double-counting tax burden in a state. This data was released in September 2012.

REMAINING TAX BURDEN

This variable was calculated by taking tax revenues from all taxes—excluding personal income, corporate income (including corporate license), property, sales, and severance per \$1,000 of personal income. We used U.S. Census Bureau Data, for which the most recent year available is 2010. This data was released in September 2012.

ESTATE OR INHERITANCE TAX (YES OR NO)

This variable assesses if a state levies an estate or inheritance tax. We chose to score states based on

either a “yes” for the presence of a state-level estate or inheritance tax, or a “no” for the lack thereof. Data was drawn from: McGuire Woods LLP, “State Death Tax Chart: Revised January 3, 2013.”

RECENTLY LEGISLATED TAX CHANGES

This variable calculates each state’s relative change in tax burden over a two-year period (in this case, 2011 and 2012), using static revenue estimates of legislated tax changes per \$1,000 of personal income. This timeframe ensures that tax changes will impact a state’s ranking long enough to overcome any lags in the tax revenue data. Laffer Associates calculations used raw data from Tax Analysts, individual state legislatures, and other sources.

DEBT SERVICE AS A SHARE OF TAX REVENUE

Interest paid on debt as a percentage of total tax revenue. This information comes from 2010 U.S. Census Bureau data.

PUBLIC EMPLOYEES PER 10,000 RESIDENTS

This variable shows the full-time Equivalent Public Employees per 10,000 of Population. This information comes from 2011 U.S. Census Bureau data.

QUALITY OF STATE LEGAL SYSTEM

This variable ranks tort systems by state. Information comes from the 2012 U.S. Chamber of Commerce State Liability Systems Ranking.

STATE MINIMUM WAGE

Minimum wage enforced on a state-by-state basis.

If a state does not have a minimum wage, we use the federal minimum wage floor. This information comes from the U.S. Department of Labor, as of January 1, 2013.

WORKERS’ COMPENSATION COSTS

This variable highlights the 2012 Workers’ Compensation Index Rate (cost per \$100 of payroll). Note: This survey is conducted by the Oregon Department of Consumer & Business Services, Information Management Division.

RIGHT-TO-WORK STATE (YES OR NO)

This variable assesses whether or not a state requires union membership for its employees. We have chosen to score states based on either a “yes” for the presence of a right-to-work law or a “no” for the lack thereof. This information comes from the National Right to Work Legal Defense and Education Foundation, Inc. Right-to-work status is as of January 1, 2013.

TAX OR EXPENDITURE LIMIT

States were ranked only by the number of state tax or expenditure limits in place. We measure this by i) a state expenditure limit, ii) mandatory voter approval of tax increases, and iii) a supermajority requirement for tax increases. One point is awarded for each type of tax or expenditure limitation a state has. All tax or expenditure limitations measured apply directly to state government. This information comes from the Cato Institute and other sources.

About the American Legislative Exchange Council

The American Legislative Exchange Council is America's largest nonpartisan, voluntary membership organization of state legislators. Made up of nearly one-third of America's state elected officials, the Council provides a unique opportunity for state lawmakers, business leaders and citizen organizations from around the country to share experiences and develop state-based, pro-growth models based on academic research, existing state policy and proven business practices. The ultimate goal of the Exchange Council is to help state lawmakers make government work more efficiently and move government closer to the communities they serve, thereby creating opportunity for all Americans.

The Process

In state legislatures around the country, citizen groups foster ideas, participate in discussions and provide their points of view to lawmakers. This process is an important part of American democracy.

The Exchange Council and its eight task forces closely imitate the state legislative process: resolutions are introduced and assigned to an appropriate task force based on subject and scope; meetings are conducted where experts present facts and opinion for discussion, just as they would in committee hearings; these discussions are followed by a vote.

Council task forces serve as testing grounds to judge whether resolutions can achieve consensus and enough support to survive the legislative process in a state capitol. All adopted model policies are published at www.alec.org to promote increased education and the open exchange of ideas across America.

The Exchange Council's Eight Task Forces and Issue Areas Include:

TASK FORCE ON CIVIL JUSTICE

- Civil Liability Predictability
- Fairness in Damages
- Discouraging Lawsuit Abuse

TASK FORCE ON COMMERCE, INSURANCE AND ECONOMIC DEVELOPMENT

- Limiting Government Mandates on Business
- Transportation and Infrastructure
- Employee Rights and Freedoms

TASK FORCE ON ENERGY, ENVIRONMENT AND AGRICULTURE

- Energy Affordability and Reliability
- Regulatory Reform
- Agriculture and Land Use

TASK FORCE ON EDUCATION

- Education Reform
- Parental Choice
- Efficiency, Accountability, and Transparency

TASK FORCE ON HEALTH AND HUMAN SERVICES

- Pro-Patient, Free Market Health Policy
- Private and Public Health Insurance
- Federal Health Reform

TASK FORCE ON INTERNATIONAL RELATIONS

- International Trade
- Intellectual Property Rights Protection
- Federalism

TASK FORCE ON TAX AND FISCAL POLICY

- Pro-Growth Tax Reform
- Priority-Based Budgeting
- Pension Reform

TASK FORCE ON COMMUNICATIONS AND TECHNOLOGY

- Broadband Deployment
- Consumer Privacy
- E-Commerce

JUSTICE PERFORMANCE PROJECT

- Recidivism Reduction
- Overcriminalization
- Data-driven criminal justice reform

"As Justice Brandeis noted, one of the happy aspects of the federal system is that a state may serve as a laboratory and try novel policy experiments. In 2012, the 'Texas Experiment' of light taxation and regulation produced more jobs than any state, and an economy growing at twice the national state average. Anyone interested in bringing similar success to their state should read this book."

U.S. Senator Ted Cruz, Texas

"I want to thank the authors of *Rich States, Poor States* and ALEC for providing policymakers and the public with this valuable resource. There is no question that states like Utah are reaping the benefits of sound fiscal policy. It is clear that limited regulation, low taxes, low debt, and balanced budgets create the best environment for business, investment, and jobs."

Senate President Wayne Niederhauser, Utah

"It is important for policymakers to have a publication that helps and encourages economic growth and competition between states to encourage prosperity. Publications like this one help educate legislators and governors with the tools to understand which policies work and which policies waste taxpayer dollars. The end goal for politicians should be the promotion of liberty, free markets, low taxation, and smaller government."

U.S. Senator Rand Paul, Kentucky

"Most state legislatures across the country are focused on reducing spending, lowering taxes, and growing their economies. *Rich States, Poor States* continues to generate in-depth policy information that is critical to making decisions that will move states in a more economically sustainable direction. This publication is an important tool for policymakers, and I consider it essential to understanding what makes each state competitive in a global economy."

Speaker Thom Tillis, North Carolina

American Legislative Exchange Council

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www.alec.org

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