NEED TO KNOW

AMERICANS FOR PROSPERITY FOUNDATION

LOW TAXES AND ECONOMIC GROWTH

Federal taxes cost the American economy more than $3 trillion in 2014 (3). States took an additional $865 billion for their coffers (4). The high cost of complying with our country's complex tax code – including tax planning, filling out paperwork, and dealing with other hassles – sapped an additional $400 billion from the economy according to estimates. All together that was more than 24 percent of our country's total economic output in 2014. Lowering these excessive tax burdens and leaving more resources in the hands of individuals, families, and businesses is a proven way to spur economic growth.

LOWER TAXES CAN DRIVE ECONOMIC GROWTH

1. Lower taxes increase the incentive to work, produce, and save – all things that contribute to economic growth. When people get to keep more of their earnings from work or from investments, putting in extra hours at work or taking on new investment risks both look relatively more attractive.

2. Lower taxes also mean less money coming out of the pockets of individuals and businesses in the private sector. When individuals and businesses get to keep more of their hard-earned dollars, they have more resources available to hire new workers, buy more goods, or invest in new equipment. It's also a boon because capital tends to be allocated more efficiently when it stays in the private sector instead of passing through government hands. For proof, look no further than the waste and duplicative spending we see regularly in government (5).

3. Lower taxes mean people waste less time and resources on legal (though unproductive) tax avoidance behavior. When facing large tax burdens, individuals and businesses tend to change their behavior and act differently instead of spending or saving as they see fit. These distortions are bad for the economy. Economists call this effect of taxation "deadweight loss."

QUICK FACTS

- A recent study sponsored by the Oklahoma Council of Public Affairs showed that gradually phasing-out the state's income tax could create 312,000 new jobs in just 10 years and save the average family of four well over $1,000 per year (1).

NOTABLE & QUOTABLE

"We can and must start to change our country's economic course by providing an environment that rewards our citizens for their efforts and their risks... The evidence is overwhelming and the proper course is clear: States should pursue policies that leave more money in our citizens' pockets to help fuel and drive our economy."

-**Sam Brownback**, Governor of Kansas (2)

THE EVIDENCE: LOWER TAXES CREATE A BETTER ECONOMIC ENVIRONMENT

Anecdotal evidence from the states bears this out. Each year, the Tax Foundation ranks all 50 states according to how competitive their tax systems are, with higher marks for low rates, less complexity, and fewer politically motivated tax preferences (6). When AFPF compared the ten states with the best tax climates with the ten states with the worst tax climates from 2000 to 2010, the results were striking. The ten best states experiences:

- 135 percent faster personal income growth;
- 445 percent more new jobs;
- 152 percent faster economic growth; and
- 299 percent faster population growth.

In other words, states with lower tax burdens had economies that were thriving, businesses that were creating more jobs, incomes and standards of living that were rising more rapidly, and people and businesses flocking to their states (probably fleeing the high-tax areas of the country).

THE UNINTENDED CONSEQUENCES OF HIGH RATES

States with lower tax burdens had more vibrant economies, faster job growth, faster personal income growth, and faster population growth than those states with high tax burdens.

In recent years, states that have raised tax rates have found little benefit from their policies. When Maryland raised tax rates on millionaires in 2008, many citizens simply moved away, bringing $1 billion of the state's net tax base along with them. Oregon increased its top income and capital gains tax rates to 11 percent in 2009, tying Hawaii for the highest rates in the nation, but officials were stunned when the number of wealthy individual tax filers plunged by a quarter and taxable capital gains fell from $3.5 billion to just $2 billion.

In 2011, Illinois raised individual and corporate tax rates by large margins. While Governors of nearby states quick made themselves "busy sending welcome letters to Illinois businesses," Illinois' state officials were busy spending the money that they were to take in from the tax hike. Two years after the tax increase, the Illinois Policy Center noted that Illinois' credit rating had been downgraded five times since the hike, that unemployment was second-highest in the nation, and that Illinois added nearly twice as many people to its food stamp rolls as there were new payroll jobs (7). That's the problem with higher rates: officials expect more revenue to fund bigger government, but individuals and businesses are forced to adjust their behavior or move when their hard-earned income is taken from them.

CONCLUSION

Even Christina Romer, former chair of the Council of Economic Advisors under President Obama, has shown that high taxes are bad economic policy: in a recent paper that she coauthored with her husband David Romer, the two Berkley economics professors find that raising taxes drives down investment and economic output (8). Pro-growth policy demands low and stable tax rates – it's as simple as that.

Endnotes

1. OFFICE OF MANAGEMENT AND BUDGET, Historical Tables of the United States Budget, Table 3.2: Outlays by Function and Subfunction (February 2011) (online at http://www.whitehouse.gov/omb/budget/Historicals).
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3. OASDI BOARD OF TRUSTEES, The 2011 Annual Report of the Board of Trustees (May 13, 2011) (online at http://www.ssa.gov/oact/tr/2011/tr2011.pdf).
4. Fleming v. Nester, 363 U.S. 603 (1960).
5. Orlo Nichols et. al, Internal Real Rates of Return Under the OASDI Program for Hypothetical Workers, SOCIAL SECURiTY ADMINISTRATION, Actuarial Note No. 2008.5 (April 2009) (online at http://www.ssa.gov/oact/NOTES/ran5/an2008-5.pdf).
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