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Solutions for Rising Costs

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Rep. Causer and members of the Committee,

Thank you for the chance to present to you this morning.

My name is Joe Bishop-Henchman and I am executive vice president at the National Taxpayers Union Foundation and an adjunct scholar at the Cato Institute. I view my job as explaining as precisely and as clearly as possible the current state of fiscal policy in light of established tax principles, so that you, the policymakers, can have the information to make informed decisions. I have worked with elected officials and stakeholders on major state-level tax changes, advised on the interplay between federal and state policy changes, and authored over 100 studies on tax policy and tax law.

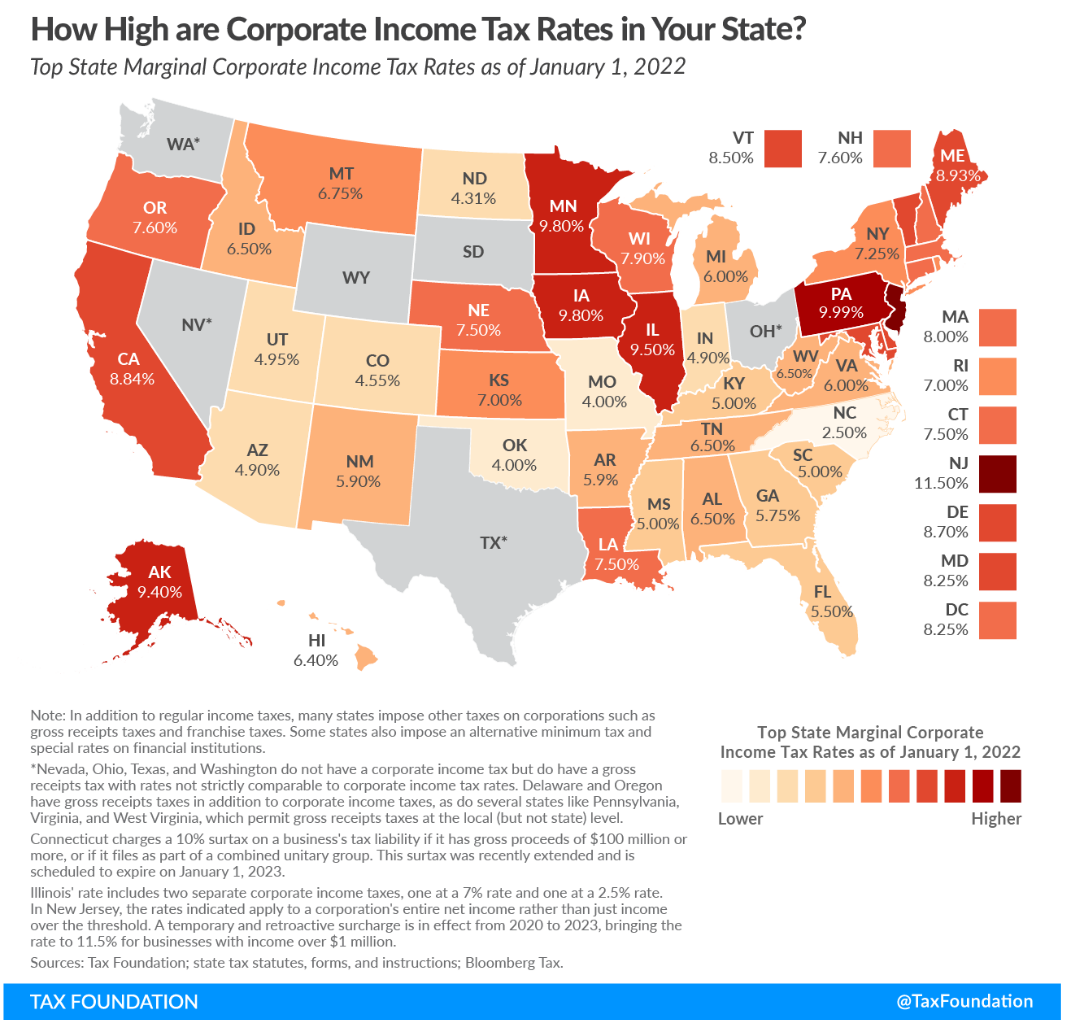
One of my first presentations in my career was in February 2008 to this committee, and it is a pleasure to be here again. In that 2008 presentation, I discussed some of the challenges to Pennsylvania's growth: a 9.99 corporate net income tax rate, a regulatory system using subsidy handouts and picking winners and losers rather than providing a level playing field for all, and Pennsylvania's opportunities and challenges with respect to federal policy and competitor states. While many years have passed and many things have changed, three points remain true and I will repeat them now:

1. Any plan that purports to improve Pennsylvania's competitiveness and future prospects which does not cut the 9.99 percent business tax is not serious.
2. Sending out checks or creating new regulations to put a thumb on the scale of innovation or competition have generally proven ineffective at achieving economic growth, and at a time of high inflation, will worsen rising costs.

3. While Pennsylvania has limited control over federal policy, it does have control over whether its policy is competitive with its neighbors and with international competitors for jobs, investment dollars, and talent.

I would like to address each of these points in turn.

Pennsylvania's 9.99 percent net corporate income tax rate is the second highest in the United States, after New Jersey's 11.5 percent rate and ahead of Minnesota's 9.8 percent. Pennsylvania is also a rare state with significant local business taxes, such as Philadelphia's 6.2 percent and gross receipts taxes in other jurisdictions, the business privilege and mercantile taxes. If you are a corporate headquarters, a manufacturer, a services center, or many other type of business looking to relocate or expand, choosing Pennsylvania means choosing some of the highest taxes in the country.



Despite the very high rate, Pennsylvania collected just $274 per capita in state and local business taxes in 2019, ninth highest in the United States. A very high "sticker rate" to collect not so much in revenue. King Louis XIV's finance minister once described taxation as the art of "plucking the goose as to obtain the largest amount of feathers with the least possible amount of hissing." Pennsylvania's tax policy is maximizing hissing (deterring business investment and expansion) without even getting a lot of feathers. New Hampshire and Delaware have higher business taxes, but also have no sales tax and other countervailing positives: New Hampshire with no income tax, and Delaware with a specialized corporate court with expertise in quickly resolving corporate matters.

The recent trend has been for reducing business taxes: in 2022, ten states adopted reductions in business taxes. Internationally, business tax burdens have been falling, with the U.S. reduction in its corporate income tax rate in 2017 being more a late-catch-up than a trend setter.

It is important to remember that although a corporate income tax is paid by a corporate treasurer, the actual economic burden of the tax is felt in the form of lower wages, increased prices, and decreased shareholder value. A corporation is just a piece of paper, usually in Delaware, and the taxes they pay are paid by real people somewhere. Reducing this tax will not only reduce this pressure for higher prices directly, it will also reduce a barrier to competition and investment that will allow prices to be lower in future years as well.

Reducing Pennsylvania's uncompetitive business taxes has long been on the wish list, and for many years the excuse has been a tight state budget that couldn't do without the short-term revenue loss. Obviously, that is less of a concern this year. Policymakers should be cautious about taking back the gains with a more expansive tax base out of step with the federal base in "return for" a rate reduction. I expect my co-panelist and friend from Washington, DC, Mr. Vermeer, will speak more to this.

Lowering regulatory burdens can do much to lower prices. Every other year, Cato Institute produces the *Freedom in the 50 States* report, ranking the states on 230 different policy variables. It is a dispassionate look at the policies with no favoritism. The 2020 report summarized Pennsylvania as follows: "Regulatory policy drags down the commonwealth's economic freedom score and is an area ripe for improvement. Pennsylvania ranks a woeful 37th on regulatory policy."

Our scholars gave several examples as contributing factors: work left to be done on tort reform and insurance liberalization, occupational licensing restrictions (particularly in nursing), state laws banning sales-below-cost or price-gouging, partisan judicial elections, the state liquor monopoly, and a civil liability system worse than the national average. In any of these areas, Pennsylvania need only do what most other states do, and that would be an improvement capable of increasing the state's competitiveness and lowering prices by reducing risk and barriers to innovation and competition. Needless to say, NTUF and Cato experts stand willing to assist with any of these policy areas should that be of interest.

Sending out checks would not alter this competitive landscape, and would be more likely to exacerbate inflationary pressures than meaningfully help people cope with them. Policymakers would be advised to take this opportunity and budgetary breathing space to tackle some of the longer-term competitive challenges that Pennsylvania faces, most of which involve reducing tax burdens and spending obligations not increasing them.

For weeks you have heard about problems, challenges, threats, warnings. I'd like to close by talking about the opportunity. This is not the first time a state has faced the need to transform from the past to the future, from one type of economy and doing business to another. Pennsylvania's tax system and regulatory system are still geared toward big businesses that can set whatever price they want and rake in the profits to pay hefty business taxes to state and local governments. That economy, if it ever existed, doesn't exist now. Pennsylvania's future growth will come from homegrown small businesses growing into large ones, innovation beating out established competitors in other states and other countries, and doing things better or cheaper than anyone else in the world. The creative and enterprising people who will make that a reality are here, now, in the state. They are in your districts and your towns. The question is: will they stay? Will they get investment when they need to grow? Will they hit a wall of obstacles and regulations and taxes or will they overcome them and be able to expand? Will they pass their businesses onto their kids or will they move with them out of state? And when similar enterprising people in other places think where will they go to grow, what will have them choose Pennsylvania?

Thank you for the opportunity to be here today.