

# POLICY WATCH

FROM THE KEYSTONE RESEARCH CENTER

## Three Tax Facts

A key assertion in the case against raising the Commonwealth's 2.8 percent personal income tax (PIT) is that a higher income tax would make Pennsylvania "uncompetitive" compared with other states.

Three facts make it clear this assertion is wrong.

**Fact 1: Pennsylvania's top income tax rate is now very low compared with other states and would remain very low if the PIT was raised to 3.4 percent.** Pennsylvania has the lowest top income tax rate of the 41 states that have an income tax. Pennsylvania would have the second lowest top income tax rate (tied with Indiana) if it raised its top rate to 3.4 percent.

**Fact 2: Even as a share of income Pennsylvania PIT payments are low relative to other**

**states and would remain low if the PIT was raised to 3.4 percent.** Pennsylvania's income taxes as a share of personal income are somewhat higher relative to other states because most Pennsylvanians pay state income taxes on *every dollar* of their income. Nevertheless, even with a rise to 3.4 percent, Pennsylvania would be just 32<sup>nd</sup> out of the 41 states with an income tax, according to projections for 2003-04 by the Department of Revenue.

**Fact 3: If Pennsylvania's income tax were raised to 3.4 percent, it would remain especially low compared with neighboring states.** As Table 1 shows, per \$1,000 of income, Pennsylvania's personal income tax with a 3.4 percent PIT rate would remain below that of every neighboring state except New Jersey.

**The bottom line:** Pennsylvania could raise the PIT from 2.8 to 3.4 percent and still have a much lower top rate than all its neighbors. The overall rate would be similar to that of New Jersey and at least 13 percent lower than Pennsylvania's other five neighbors.

### Taxes Support Competitiveness Too

Economic growth depends as much on adequate public services as low taxes. Testifying before the U.S. Senate, Paul O'Neil, former CEO of Alcoa and former Secretary of the Treasury said that "As a businessman, I never made an investment decision based on the Tax Code . . ."<sup>1</sup>

State	2003-04 PIT per \$1,000 of Personal Income	2002 Highest Marginal Tax rate
Delaware	\$26.81	5.95%
Maryland	\$24.41	4.75%
New Jersey	\$20.97	6.37%
New York	\$29.79	6.85%
Ohio	\$24.32	7.50%
West Virginia	\$24.81	6.50%
PA PIT @ 3.4%	\$21.17	3.40%
PA PIT @ 3.2%	\$20.01	3.20%

Sources: Personal income tax estimates provided by the Pennsylvania Department of Revenue (DOR). Personal income estimated by DOR based on Bureau of Economic Analysis 2002. Marginal rates: Tax Foundation.

Cutting taxes to the point where government cannot provide the public goods that support economic growth — such as a well-educated workforce and adequate infrastructure — will be as destructive to competitiveness as high taxes.

The fact is that Pennsylvania has been cutting business taxes for the last decade and still has one of the worst job creation records in the nation.

The verdict of the market seems clear enough: tax cutting, by itself, won't make Pennsylvania more competitive. A modest rise in the PIT to 3.4 percent could make the state **more** competitive by allowing it to provide public services that will, in the long run, build a solid foundation for sustained economic growth.

<sup>1</sup> Paul O'Neil, Senate Confirmation Hearing for Treasury Secretary, January 17, 2001.

Policy Watch is issued periodically by the

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