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Tax Cut Update

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At least 21 states have already enacted tax cuts this year, and several more reductions are likely to be adopted before the books are closed on this year's legislative sessions. But, from the perspective of the overall state budgets, the great majority of tax reductions are little more than tokens. They allow governors and legislators to claim the mantle of tax cutters, but they will not put much of a dent in state tax collections, nor will they reduce the payments of most taxpayers much.

Many of the cuts are being gradually phased in over a period of years. This is true, for example, of the exemption of groceries from the sales tax in Georgia. Half of the tax comes off in October, but the remainder will not be removed until next year. The Georgia tax cut is probably the largest in the country as a proportion of state tax revenue.

By far the most common type of tax cut was for certain businesses. At least 13 states cut business taxes. In seven of these states, these were the only tax cuts. In most states, the reductions are not across-the-board. Rather, they benefit only select businesses.

Most of the personal income tax cuts were modest. For example, the Ohio legislature raised the personal income tax exemption $100 per year for two additional years. The only states cutting income tax rates were Delaware and Utah. Kentucky raised the standard deduction, Iowa liberalized indexing provisions, Oklahoma boosted an exemption for pension income, New Jersey allowed the deduction for property taxes that most other states permit, and Michigan provided a one-time rebate.

No compilation is available yet of how much this year's tax cuts amount to, but it is surely much less than the $4 billion in reductions last year. That reduction itself amounted to only about 1 percent of total state tax revenue.

The modest size of 1996 tax cuts is evidence of widespread caution in state capitals. Governors and legislators are still waiting to see whether the federal government shifts costly responsibilities to them next year. Many states have apparently accumulated large balances because of their cautious fiscal policies and stronger than expected tax revenue this Spring.

Many states are still phasing in tax cuts enacted last year, making it more difficult for them to reduce taxes in 1996.

Among the other states that still may reduce business taxes are California, Massachusetts (by changing the rules for apportioning income of financial institutions), New York, and North Carolina.

For the second consecutive year, there were apparently no large tax increases.

The long-term significance of this year's tax actions is uncertain. Because their budgets were in good shape, most states were able to increase spending enough to maintain services, cut taxes slightly, and hold balances for future years. The real test of state tax policy will come when state fiscal conditions deteriorate and states face a choice between cutting services deeply and raising taxes.

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States Cutting Taxes in 1996

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This is a compilation of state tax reductions enacted this year as of July 3. Although most states have completed their legislative sessions, a few state legislatures are still meeting or may return for special sessions, perhaps adding to the list of states with tax cuts. This list does not count tax cuts passed in 1995 that take effect or phase in this year. The only state that increased taxes much is apparently Hawaii, where the state budget faced an impending deficit due to a weak economy.

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Colorado Insurance premium tax; child care credit
Connecticut Business taxes
Delaware Personal income tax; business taxes
Florida  Business taxes
Georgia  Sales tax on food; intangibles tax
Indiana  Taxes on homes and cars
Iowa  Property tax; income tax indexing
Kentucky Increased standard deduction on income tax, reduced   provider tax on doctors
Louisiana Business taxes
Maine  Nursing homes
Maryland Snack tax
Michigan* Income tax rebate due to tax cap; business tax; increased   dividend and interest exemption for senior citizens
New Jersey Permitted deduction of property tax payments on personal   income tax
Ohio  Increased income tax personal exemption $100 in 1998 and   again in 1999 (Such increases are already scheduled for   1996 and 19
Oklahoma Targeted business tax cuts, higher exemption for pension    income
Pennsylvania Business tax cut (job credit)
South Carolina Manufacturing property tax
Utah  Personal income tax and state property tax; also narrowed   sales tax base
Virginia Business, professional, occupational license tax
Washington Business tax cuts
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West Virginia Franchise tax; new personal income tax exemption for low- income households

* Tax cut was signed by governor in 1996 but had already passed the legislature in December 1995.

Other Publications by the Authors

- Steven D. Gold