

## Pennsylvania Tax Policy in a National Context

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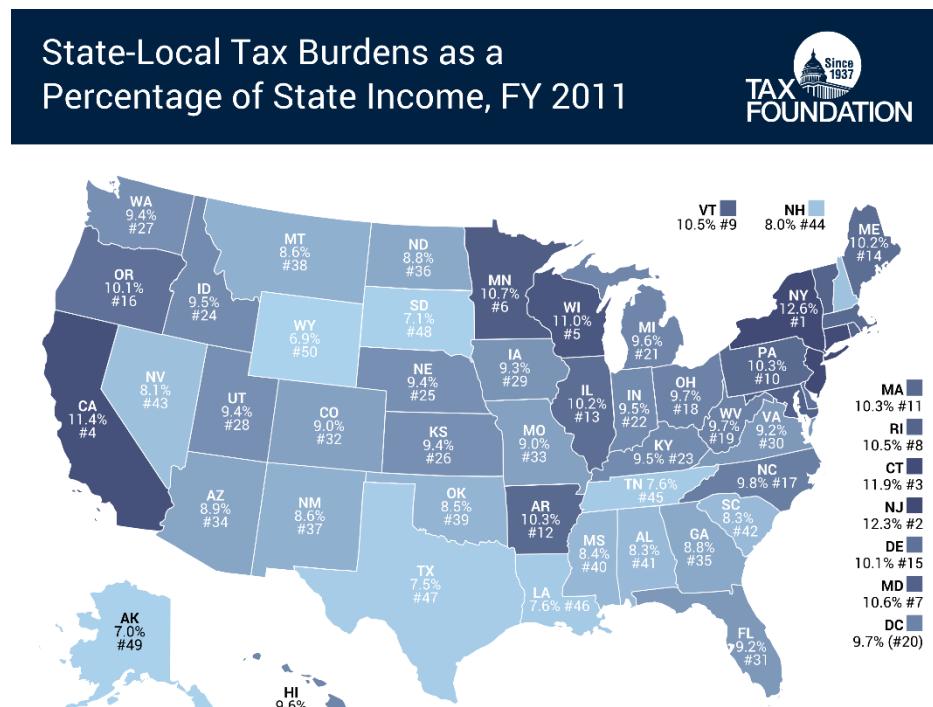
York College of Pennsylvania

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### Introduction

Since 1937, the Tax Foundation has monitored tax policy at the federal, state, and local levels. We have produced the *Facts & Figures* handbook since 1941, we calculate *Tax Freedom Day* each year, and we rank the states in our popular *State Business Tax Climate Index*.

Below, I will walk through our findings on Pennsylvania's tax policy in a national context, making note of recent legislative efforts and recommending policy reforms for consideration.



### How Much Are We Paying?

Our *State-Local Tax Burdens* report is a ranking that measures how much is being paid by taxpayers in each state. Pennsylvania ranks as a high-burden state: in fiscal year 2011, taxpayers paid 10.3 percent of their income in state and local taxes, 10<sup>th</sup> highest in the nation.

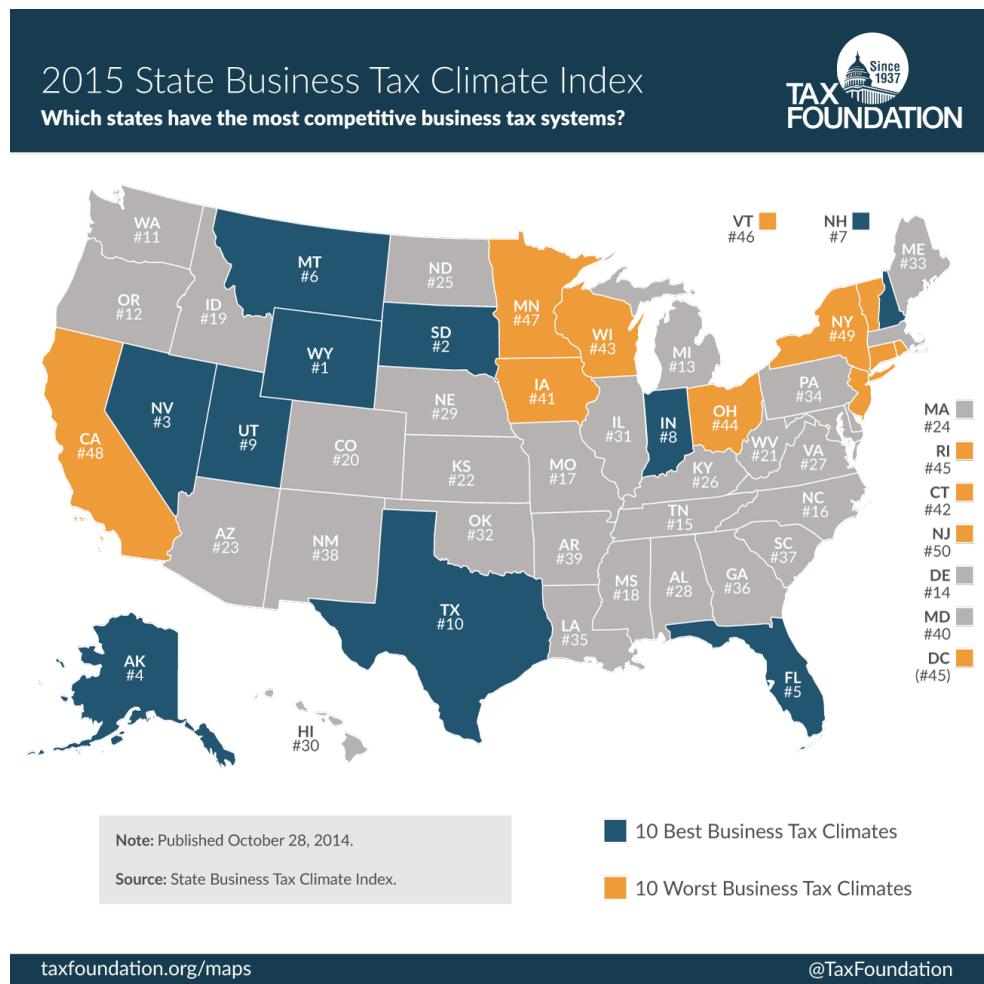
State and Local Tax Burden  
as a Percentage of State Income



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## How Well Are Taxes Structured?

Our State Business Tax Climate Index measures the quality of each state's tax code, comparing states on more than one hundred variables that rank the code's simplicity, neutrality, and competitiveness. In 2015, Pennsylvania ranked toward the bottom of the pack, at 34<sup>th</sup> best in the country.



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## Pennsylvania's Tax System is a Mixed Bag

Breaking apart the component tax types that we measure in our Index, we can get a better idea of which parts of Pennsylvania's code are well-structured, and which parts need improvement (Table 1). The state's corporate income tax, for example, has the second highest rate in the country, at 9.99 percent. When added to the federal corporate tax, Pennsylvania corporations face a top marginal rate of 44.99 percent. When tax base elements are included, the corporate tax structure ranks 46<sup>th</sup> nationally.

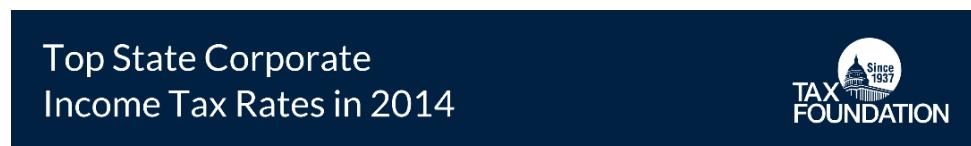
Property taxes in Pennsylvania also rank poorly. While property tax collections are a moderate \$1,305 per capita (26<sup>th</sup> highest nationally), the state levies many taxes on accumulated wealth that don't exist in other states: the inheritance tax tops out at 15 percent, and the capital stock tax was supposed to phase out by 2014, but the phase out has been extended.

Table 1: State Business Tax Climate Index Component Tax Scores, 2015

By contrast, the individual income tax in Pennsylvania is one of the better-structured systems in the United States. The 3.07 percent rate is the same across the board, and has been consistent for many years. Local income tax rates can add on a substantial burden though, with the rate in Harrisburg tolling an additional 2 percent, and the rate in Philadelphia reaching 3.928 percent.

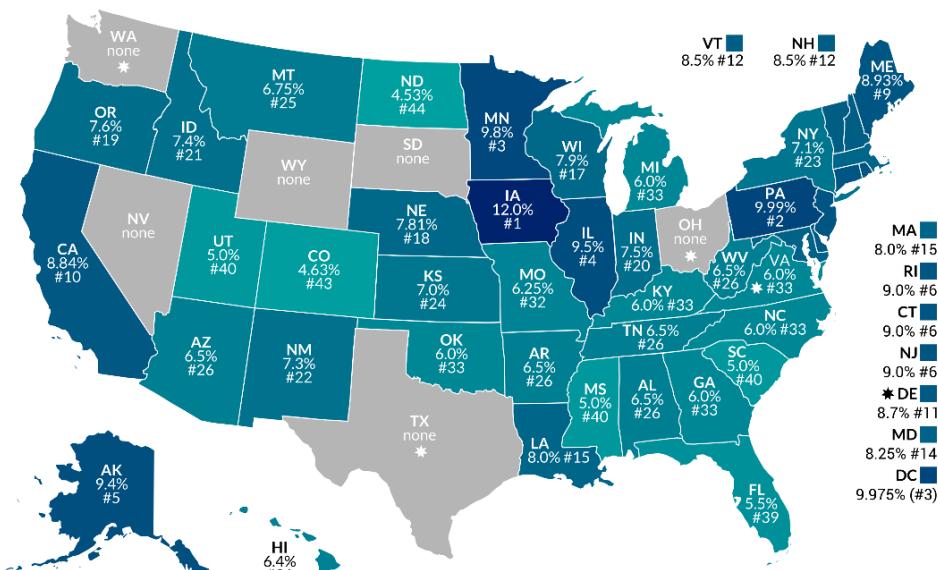
Finally, the state levies some of the highest unemployment insurance taxes in the country, and our ranking shows the total structure as being the worst nationally.

	RANK
OVERALL	34 <sup>th</sup>
CORPORATE	46 <sup>th</sup>
INDIVIDUAL	17 <sup>th</sup>
SALES	24 <sup>th</sup>
UNEMPLOYMENT INSURANCE	50 <sup>th</sup>
PROPERTY	42 <sup>nd</sup>



### Making Pennsylvania Competitive

Pennsylvania's corporate tax rate is one of the most striking features of the tax system, and should be the prime focus of legislators in the next session. The 9.99 percent rate puts Pennsylvania companies at a disadvantage nationally and globally.



**Note:** Connecticut's rate includes a 20% surtax. Illinois's rate includes two separate corporate income taxes. Data as of Jan 1, 2014. Published Apr 15, 2014.

**Sources:** State tax statutes, forms, and instructions; Commerce Clearinghouse.



\* State has gross receipts taxes with rates not strictly comparable to corporate income tax rates.

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According to the academic literature, corporate taxes are the most

harmful taxes to economic growth<sup>1</sup>, but they are a smaller part of the revenue toolkit than is often understood. In fiscal year 2011, for example, state corporate income taxes brought in just 4.1 percent of state-local tax collections. Cutting the corporate rate, then, is a relatively high bang-for-your-buck proposition, because it does not cost a lot of revenue. The capital stock tax also increases the cost of doing business in the state, and the delay in its phase out is a poor stopgap measure for additional revenue.

Finally, the inheritance tax has seen various exclusions for different types of family businesses in the past few years, notably for farmers. The trend in states today is away from estate and inheritance taxes: in just the last two years, Indiana and North Carolina have repealed theirs, and Maryland, Minnesota, New York, Rhode Island, and the District of Columbia have all increased their exemptions. Pennsylvania should consider full repeal of its inheritance tax, as it only made up 2.9 percent of general fund revenue in fiscal year 2012.<sup>2</sup>

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#### **ABOUT THE TAX FOUNDATION**

The Tax Foundation is the nation's leading independent tax policy research organization. Since 1937, our principled research, insightful analysis, and engaged experts have informed smarter tax policy at the federal, state, and local levels.

#### **ABOUT THE CENTER FOR STATE TAX POLICY AT THE TAX FOUNDATION**

The Tax Foundation's Center for State Tax Policy produces and markets timely and high-quality data, research, and analysis on state fiscal issues that influence the debate toward economically principled tax policies. Our experts are routinely relied upon for presentations, testimony, and media appearances on state tax and fiscal policy, and our website is a comprehensive resource for information on tax and spending policy in each state.

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<sup>1</sup> William McBride, *What Is the Evidence on Taxes and Growth?*, TAX FOUNDATION SPECIAL REPORT No. 207 (Dec.18, 2012), <http://taxfoundation.org/article/what-evidence-taxes-and-growth>.

<sup>2</sup> Governor's Executive Budget, 2013-14, p.C1-11.