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2010 State Business Tax Climate Index

By
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Introduction

The Tax Foundation presents the 2010 State Business Tax Climate Index (hereafter the SBTCI or the Index) as a tool for lawmakers, businesses and individuals alike to gauge how their states' tax systems compare. Policymakers can use the SBTCI to pinpoint changes to their tax systems that will explicitly improve their states' standing in relation to competing states.

American companies often function at a competitive disadvantage in the global economy. They pay one of the highest corporate tax rates of any of the industrialized countries. The top federal rate on corporate income is 35 percent, and states with punitive tax systems cause companies to be even less competitive globally.

The modern market is characterized by mobile capital and labor. Therefore, companies will locate where they have the greatest competitive advantage. States with the best tax systems will be the most competitive in attracting new businesses and most effective at generating economic and employment growth.

Although the market is now global, the Department of Labor reports that most mass job relocations are from one U.S. state to another rather than to an overseas location.[1] Certainly job creation is rapid overseas, as previously underdeveloped nations enter the world economy. So state lawmakers are right to be concerned about how their states rank in the global competition for jobs and capital, but they need to be more concerned with companies moving from Ithaca, NY, to Indianapolis, IN, than from Ithaca to India. This means that state lawmakers must be aware of how their states' tax climates match up to their immediate neighbors and to other states within their regions.

State lawmakers are always mindful of their states' business tax climates, but they are often tempted to lure business with lucrative tax incentives and subsidies instead of broad-based tax reform. This can be a dangerous proposition as a case in Florida illustrates. In July of 2004 Florida lawmakers cried foul because a major credit card company announced it would close its Tampa call center, lay off 1,110 workers, and outsource those jobs to another company. The reason for the lawmakers' ire was that the company had been lured to Florida with a generous tax incentive package and had enjoyed nearly $3 million worth of tax breaks during the previous nine years.[2] Another example comes from *USA Today* article chronicled that similar problems other states are having

1 U.S. Department of Labor, "Extended Mass Layoffs in the First Quarter of 2007," August 9, 2007, located at http://www.bls.gov/opub/ted/2007/may/wk2/art04.htm . In the press release, DOL reported that, "In the 61 actions where employers were able to provide more complete separations information, 84 percent of relocations (51 out of 61) occurred among establishments within the same company. In 64 percent of these relocations, the work activities were reassigned to place elsewhere in the U.S. Thirty six percent of the movement-of-work relocations involved out-of-country moves (22 out of 50).

2 Dave Wasson, "Florida Lawmakers Slam Capital One's Layoff After Years of Tax Breaks," Tax Analysts, July 24, 2004.

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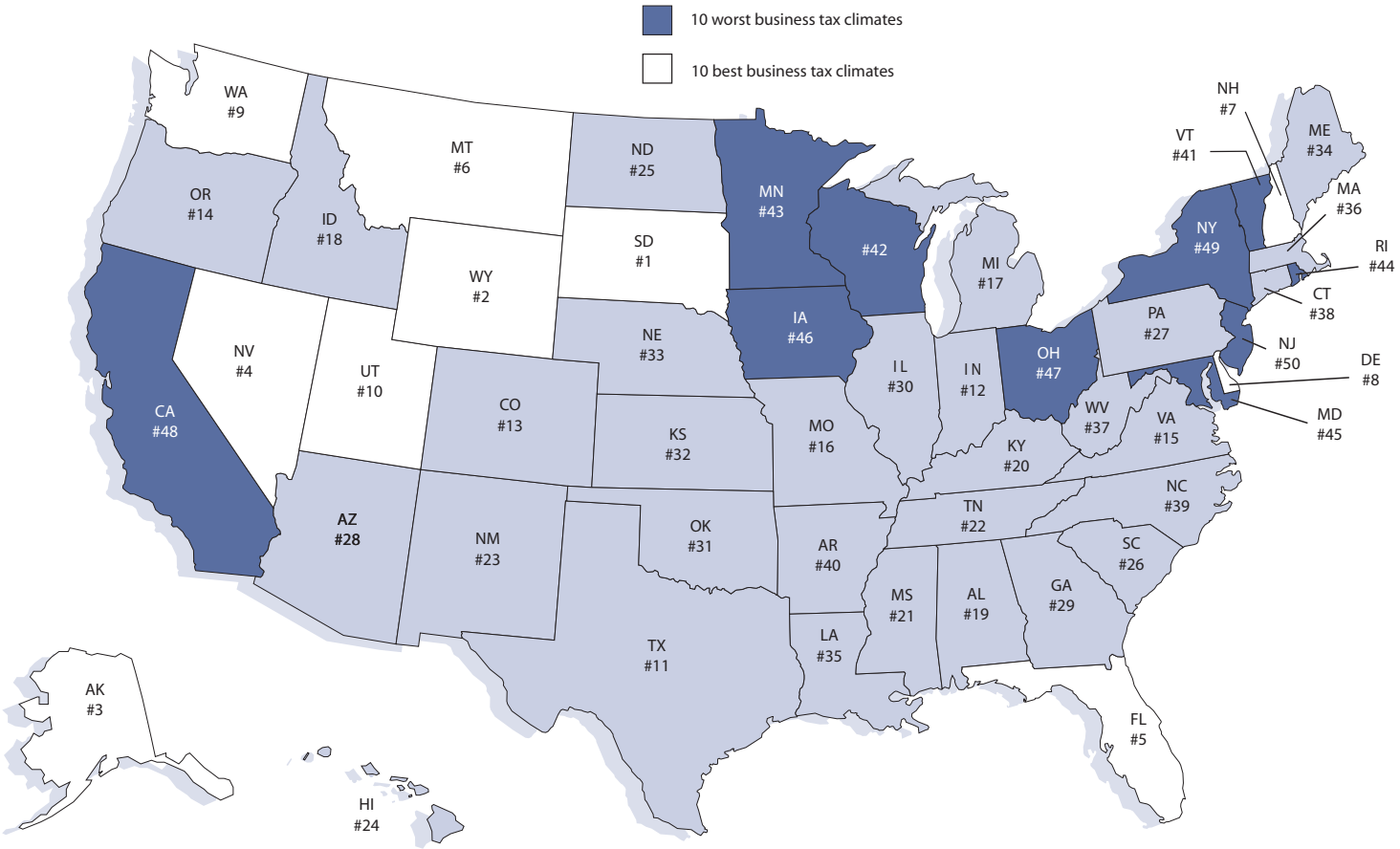
with companies who receive generous tax incentives.[3]

Lawmakers create these deals under the banner of job creation and economic development, but the truth is that if a state really can't attract employers without such packages, it is often because punitive tax laws have created a woeful business tax climate. Alas, it's a vicious cycle. States give away tax revenue to new businesses, creating pressure for higher tax rates; and the higher the state's statutory tax rates, the more important special packages become. A far more effective approach is to systematically improve the business tax climate for the long term so as to improve the state's competitiveness. When assessing which changes to make, lawmakers need to remember these two rules:

1. Taxes matter to business. Business taxes affect business decisions, job creation and retention, plant location, competitiveness, the transparency of the tax system, and the long-term health of a state's economy. Most importantly, taxes diminish profits. If taxes take a larger portion of profits, that cost is passed along to either consumers (through higher prices), workers (through lower wages or fewer jobs), or shareholders (through lower dividends or share value). Thus, a state with lower tax costs will be more attractive to business investment, and more likely to experience economic growth.
2. States do not enact tax changes (increase or cuts) in a vacuum. Every tax law will in some way change a state's competitive position relative to its immediate neighbors, its geographic region, and even globally. Ultimately it will affect the state's national standing as a place to live and to do business. Entrepreneurial states can take advantage of the tax increases of their neighbors to lure businesses out of high-tax states.

Figure 1

State Business Tax Climate Index, Fiscal Year 2010



3 Dennis Cauchon, "Business Incentives Lose Luster for States," USA Today, August 22, 2007

Clearly, there are many non-tax factors that affect a state's overall business climate: its proximity to raw materials or transportation centers, its regulatory or legal structures, the quality of its education system and the skill of its workforce, not to mention the intangible perception of a

Table 1
State Business Tax Climate Index, 2006 – 2010

	FY 2010 State Business Tax Climate Index		FY 2009 State Business Tax Climate Index		Change from 2009 to 2010		FY 2008 State Business Tax Climate Index		FY 2007 State Business Tax Climate Index		FY 2006 State Business Tax Climate Index	
State	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank
U.S.	5.00	–	5.00	–	0	–	5.00	–	5.00	–	5.00	–
Alabama	5.19	19	5.30	20	–0.11	1	5.08	23	5.16	22	5.60	16
Alaska	7.38	3	7.32	4	0.06	1	7.13	3	6.99	4	7.29	3
Arizona	5.01	28	5.25	24	–0.23	–4	5.01	25	4.95	29	5.13	29
Arkansas	4.61	40	4.87	35	–0.25	–5	4.65	37	4.72	36	4.87	35
California	3.89	48	4.14	48	–0.11	1	3.93	49	3.92	48	4.64	42
Colorado	5.63	13	5.89	13	–0.26	0	5.89	10	5.90	11	5.70	13
Connecticut	4.72	38	4.81	37	–0.09	–1	4.60	38	4.69	39	4.66	41
Delaware	5.98	8	6.01	10	–0.02	2	6.09	9	6.11	8	6.10	9
Florida	6.62	5	6.92	5	–0.30	0	6.67	5	6.79	5	6.85	5
Georgia	5.01	29	5.16	27	–0.15	–2	4.95	28	5.18	21	5.52	20
Hawaii	5.05	24	5.27	22	–0.22	–2	5.27	18	5.34	16	5.28	24
Idaho	5.21	18	5.10	29	0.11	11	5.09	22	5.05	26	5.08	30
Illinois	5.01	30	5.26	23	–0.26	–7	5.04	24	4.92	31	5.22	26
Indiana	5.67	12	5.88	14	–0.20	2	5.65	13	5.72	12	5.86	12
Iowa	4.23	46	4.35	44	–0.12	–2	4.16	46	4.36	45	4.62	44
Kansas	4.93	32	5.07	31	–0.14	–1	4.87	31	4.77	35	4.99	33
Kentucky	5.18	20	4.95	34	0.23	14	4.98	27	4.96	28	4.75	38
Louisiana	4.74	35	4.98	33	–0.24	–2	4.75	34	4.79	33	5.05	32
Maine	4.83	34	4.69	40	0.14	6	4.72	35	4.72	37	4.64	43
Maryland	4.26	45	4.31	45	–0.06	0	4.14	47	5.08	24	5.23	25
Massachusetts	4.73	36	4.99	32	–0.26	–4	4.80	33	4.79	34	4.87	36
Michigan	5.35	17	5.30	21	0.05	4	5.32	17	5.14	23	5.20	28
Minnesota	4.44	43	4.61	41	–0.18	–2	4.40	42	4.39	43	4.71	39
Mississippi	5.16	21	5.32	19	–0.16	–2	5.09	22	5.21	19	5.57	19
Missouri	5.37	16	5.57	16	–0.20	0	5.35	16	5.37	15	5.68	14
Montana	6.32	6	6.27	6	0.05	0	6.35	6	6.42	6	6.16	8
Nebraska	4.88	33	4.55	42	0.32	9	4.55	40	4.55	41	4.59	45
Nevada	7.05	4	7.37	3	–0.31	–1	7.07	4	7.07	3	7.07	4
New Hampshire	6.25	7	6.21	7	0.05	0	6.29	7	6.32	7	6.45	6
New Jersey	3.60	50	3.90	50	–0.30	0	3.71	50	3.68	50	3.63	48
New Mexico	5.06	23	5.17	26	–0.11	3	4.93	29	5.05	25	5.30	23
New York	3.66	49	4.00	49	–0.47	–2	4.19	45	4.29	46	3.60	49
North Carolina	4.66	39	4.74	39	–0.08	0	4.52	41	4.52	42	4.70	40
North Dakota	5.04	25	5.08	30	–0.04	5	4.86	32	4.87	32	5.06	31
Ohio	4.04	47	4.15	47	–0.08	1	3.95	48	3.95	47	3.82	47
Oklahoma	4.97	31	5.40	18	–0.43	–13	5.18	19	5.20	20	5.41	21
Oregon	5.59	14	6.04	8	–0.44	–6	6.12	8	6.06	9	6.02	10
Pennsylvania	5.03	27	5.14	28	–0.10	1	4.92	30	4.95	30	5.31	22
Rhode Island	4.33	44	4.18	46	0.15	2	4.20	44	3.80	49	3.47	50
South Carolina	5.03	26	5.21	25	–0.17	–1	5.01	26	4.98	27	5.21	27
South Dakota	7.42	1	7.50	2	–0.08	1	7.21	2	7.18	2	7.56	2
Tennessee	5.10	22	5.42	17	–0.32	–5	5.16	20	5.27	17	5.58	18
Texas	5.70	11	6.02	9	–0.32	–2	5.79	11	5.99	10	6.41	7
Utah	5.80	10	5.94	11	–0.14	1	5.71	12	5.23	18	5.67	15
Vermont	4.56	41	4.52	43	0.03	2	4.34	43	4.37	44	4.57	46
Virginia	5.53	15	5.70	15	–0.17	0	5.51	15	5.51	14	5.58	17
Washington	5.81	9	5.94	12	–0.13	3	5.65	14	5.67	13	5.93	11
West Virginia	4.73	37	4.86	36	–0.13	–1	4.66	36	4.71	38	4.93	34
Wisconsin	4.54	42	4.76	38	–0.22	–4	4.56	39	4.57	40	4.77	37
Wyoming	7.38	2	7.50	1	–0.12	–1	7.24	1	7.46	1	7.64	1
District of Columbia	4.72	–	4.53	–	0.20	–	4.53	–	4.49	–	4.06	–

Note: The higher the score, the more favorable a state's tax system is for business. All scores are for fiscal years.
Source: Tax Foundation

state's "quality of life."[4] The 2010 SBTCI does not measure the impact of these important features of a state's overall business climate. Rather, the SBTCI merely seeks to measure the tax component of each state's business climate.

Some of the non-tax factors of a state's business climate are outside of the control of elected officials. Montana lawmakers cannot change the fact that Montana's businesses have no immediate access to deepwater ports. Lawmakers do, however, have direct control over how friendly their tax systems are to business. Furthermore, unlike changes to a state's health care, transportation or education system, which can take decades to implement, changes to the tax code bring almost instantaneous benefits to a state's business climate.

The ideal tax system, whether at the local, state or federal level, is simple, transparent, stable, neutral to business activity, and pro-growth. In such an ideal system, individuals and businesses would spend a minimum amount of resources to comply with the tax system, understand the true cost of the tax system, base their economic decisions solely on the merits of the transactions, without regard to tax implications, and not have the tax system impede their growth and prosperity.

In reality, tax-induced economic distortions are a fact of life, and a more realistic goal is to maximize the occasions when people's economic decisions, whether in business or personal life, are guided by their own judgments, and minimize those cases where economic decisions are micromanaged or even dictated by a tax system. Therefore, the most competitive tax systems, and the ones that score best in the SBTCI, are those that create the fewest economic distortions by enforcing the most simple, pro-growth tax systems characterized by broad bases and low rates.

The SBTCI does not measure business tax burdens. While it is unquestionably important how much revenue states collect in business taxes, the manner in which they extract tax revenue is also important. In other words, quite apart from whether a state's total business tax burden is higher than in other states, it can enact (and many states do) a set of business tax laws that cause great damage to the economy. The SBTCI does not allow states with poor business tax regimes to hide behind low business tax burdens.

Good state tax systems levy low, flat rates on the broadest bases possible, and they treat all taxpayers the same. Variation in the tax treatment of different industries favors one economic activity or decision over another. The more riddled a tax system is with politically motivated preferences the less likely it is that business decisions will be made in response to market forces. The SBTCI rewards those states that apply these principles in five important areas of taxation: major business taxes, individual income taxes, sales taxes, unemployment insurance taxes and property taxes.

Tax competition is an unpleasant reality for state revenue and budget officials, but it is an effective restraint on state and local taxes. It also helps to more efficiently allocate resources because businesses can locate in the state where they receive the services they need at the lowest cost. When a state imposes higher taxes than a neighboring state, businesses will cross the border to some extent. Therefore states with more competitive tax systems score well in the SBTCI because they are best suited to generate economic growth.

Ranking the competitiveness of 50 very different tax systems presents many challenges, especially when a state dispenses with a major tax entirely. Should Utah's tax system which includes three relatively neutral taxes on general sales, individual income and corporate income be considered more or less competitive than Alaska's tax system, which includes a particularly burdensome corporate income tax but no tax on individual income or general statewide sales?

The 2010 SBTCI deals with such questions by comparing the states on five separate aspects of their tax systems and then adding the results up to a final, overall ranking. This approach has the advantage of rewarding states on particularly strong aspects of their tax systems (or penalizing them on particularly weak aspects) while also measuring the general competitiveness of their overall tax systems. The results are a score that can be compared to other states' scores. Ultimately, both Alaska and Utah score well.

This edition is the 2010 SBTCI and represents the tax climate of each state as of July 1, 2009, the first day of the standard 2010 fiscal year.

4 A trend in tax literature through the 1990s has been the increasing use of indexes to measure a state's general business climate. These include the Center for Policy and Legal Studies' "Economic Freedom in America's 50 States: A 1999 Analysis" and the Beacon Hill Institute's "Eighth Annual State Competitiveness Report." Such indexes even exist on the international level, including the Heritage Foundation/*Wall Street Journal's* "2009 Index of Economic Freedom." Plaut and Pluta (1983) examined the use of business climate indexes as explanatory variables for business location movements. They found that such general indexes do have a significant explanatory power, helping to explain, for example, why businesses have moved from the Northeast and Midwest towards the South and Southwest. In turn, they also found that high taxes have a negative effect on employment growth.

The Best and Worst Business Tax Climates

The ten best states in the Tax Foundation's 2010 State Business Tax Climate Index are as follows:

1. South Dakota
2. Wyoming
3. Alaska
4. Nevada
5. Florida
6. Montana
7. New Hampshire
8. Delaware
9. Washington
10. Utah

It is obvious that the absence of a major tax is a dominant factor in vaulting these ten states to the top of the ranking. Property taxes and unemployment insurance taxes are levied in all 50 states, but there are 12 states that do without one or more of the other major taxes: the corporate tax, the individual income tax, or the sales tax. Wyoming, Nevada and South Dakota have no corporate or individual income tax; Alaska has no individual income or state-level sales tax; Florida and Texas have no individual income tax; and New Hampshire, Delaware, Oregon and Montana have no sales tax.

The lesson is simple; a state that raises sufficient revenue without one of the major taxes will, all things being equal, out-compete those states that levy every tax in the state tax collector's arsenal.

The ten states whose tax systems are most inhospitable to economic growth are as follows:

41. Vermont
42. Wisconsin
43. Minnesota
44. Rhode Island
45. Maryland
46. Iowa
47. Ohio
48. California
49. New York
50. New Jersey

Most states have at least one major tax area that is hospitable to business and economic growth, and most have at least one punitive tax that makes the state's tax climate look comparatively bad. For example, California ranks poorly overall, 48th best, despite having the 13th best score on property taxes. On the other end of the spectrum, Delaware ranks 8th best despite a dreadful corporate income tax that ranks as the second worst in the nation.

On the other hand, some states do manage to achieve an almost uniformly good or poor tax climate. New Jersey has only one tax that scores dead last, property taxes, but its overall ranking is 50th because it has no competitive taxes. The best it can muster is a middle-of-the-pack 25th on unemployment insurance, the least heavily weighted sub-index, while scoring poorly on the three biggest state-level taxes: corporate income (10th worst), personal income (4th worst) and general sales (13th worst).

On the other hand, Montana's tax system is uniformly good and ranks 6th best overall. Its zero sales tax rate assures a top ranking, but it has maintained a competitive posture in other areas too: 16th best on corporate income, 23rd best on personal income, 21st best on unemployment insurance and 10th best on property taxes.

Detailed descriptions of each component index, each sub-index, and their various components is presented later in the paper and those states that score especially well or poorly on each component are discussed to provide guidance on the changes that each state might well contemplate.

A Review of the Economic Literature

Economists have not always agreed on how individuals and businesses react to taxes. As early as 1956, Charles Tiebout postulated that if citizens were faced with an array of communities that offered different types or levels of public goods and services at different costs or tax levels, then all citizens would choose the community that best satisfied their particular demands, revealing their preferences by "voting with their feet." Tiebout's article is the seminal work on the topic of taxation's effect on the location decisions of taxpayers.

Tiebout also suggested that citizens with high demands for public goods would concentrate themselves in communities with high levels of public services and high taxes while those with low demands would choose communities with low levels of public services and low taxes. Competition among jurisdictions results in a variety of communities, each with residents that receive all public services similarly.

However, businesses sort out the costs and benefits of taxes differently from individuals. To businesses, which can be more mobile and must earn profits to justify their existence, taxes reduce profitability. Theoretically, then, businesses could be expected to be more responsive than individuals to the lure of low-tax jurisdictions.

The economic literature over the past 50 years has slowly cohered around this hypothesis. Ladd (1998) summarizes the post-World War II empirical tax research literature in an excellent survey article, breaking it down into three distinct

periods of differing ideas about taxation: 1) taxes do not change behavior; 2) taxes may or may not change business behavior depending on the circumstances; 3) taxes definitely change behavior.

Period one, with the exception of Tiebout, included the 1950s, '60s and '70s and is summarized succinctly in three survey articles: Due (1961), Oakland (1978) and Wasylenko (1981). Due's was a polemic against tax giveaways to businesses, and his simple analysis techniques consisted of basic correlations, interview studies and the examination of taxes relative to other costs. He found no evidence to support the notion that taxes influence business location.

Oakland was skeptical of the assertion that tax differentials at the local level had no influence at all. However, because econometric analysis was relatively unsophisticated at the time, he found no significant articles to support his intuition. Wasylenko's survey of the literature found some of the first evidence indicating that taxes do influence business location decisions. However, the statistical significance was lower than that of other factors such as labor supply and agglomeration economies. Therefore, he dismissed taxes as a secondary factor at most.

Period two was a brief transition during the early to mid-1980s. This was a time of great ferment in tax policy as Congress passed major tax bills, including the so-called Reagan tax cut in 1981 and a dramatic reform of the tax code in 1986. Articles revealing the economic significance of tax policy proliferated and became more sophisticated. For example, Wasylenko and McGuire (1985) extended the business location literature to non-manufacturing sectors and found, "Higher wages, utility prices, personal income tax rates, and an increase in the overall level of taxation discourage employment growth in several industries." However, Newman and Sullivan (1988) still found a mixed bag in their observation that significant tax effects [only] emerged when models were carefully specified" (Ladd, p.89).

Ladd was writing in 1998, so her "period three" started in the late 1980s and continued up to 1998 when the quantity and quality of articles increased significantly. Articles that fit into period three begin to surface as early as 1985, as Helms (1985) and Bartik (1985) put forth forceful arguments based on empirical research that taxes guide business decisions. Helms concluded that a state's ability to attract, retain, and encourage business activity is significantly affected by its pattern of taxation. Furthermore, tax increases significantly retard economic growth when the revenue is used to fund transfer payments. Bartik found that the conventional view, as he describes it, that state and local taxes have little effect on business is false.

Papke and Papke (1986) found that tax differentials between locations may be an important business location factor, finding that consistently high business taxes can represent a hindrance to the location of industry. Interestingly, they use the same type of after-tax model used by Tannenwald (1996) who reaches a different conclusion.

Bartik (1989) provides strong evidence that taxes negatively impact business start-ups. He finds specifically that property taxes, because they are paid regardless of profit, have the strongest negative effect on business. Bartik's econometric model also predicts that tax elasticities of –0.1 to –0.5 imply that a ten percent cut in tax rates will increase business activity by 1 to 5 percent. Bartik's findings about property taxation, as well as those of Mark, McGuire and Papke (2000), buttress the argument for inclusion of a a sub-index in the SBTCI devoted to taxes on real property and other assets.

By the early 1990s, the literature expanded enough so that Bartik (1991) found 57 studies on which to base his literature survey. Ladd succinctly summarizes Bartik's findings:

> The large number of studies permitted Bartik to take a different approach from the other authors. Instead of dwelling on the results and limitations of each individual study, he looked at them in the aggregate and in groups. Although he acknowledged potential criticisms of any particular study, he convincingly argued that some systematic flaw would have to cut across all studies for the consensus results to be invalid. In striking contrast to previous reviewers, he concluded that taxes have quite large and significant effects on business activity" (p. 92).

Ladd's "period three" surely continues to this day. Agostini and Tulayasatheien (2001) examined the effects of corporate income taxes on the location of foreign direct investment in U.S. states. They determined that for "foreign investors, the corporate tax rate is the most relevant tax in their investment decision." Therefore, they found that foreign direct investment was quite sensitive to states' corporate tax rates (p. 28).

Mark, McGuire and Papke (2000) find that taxes are a statistically significant factor in private-sector job growth. Specifically, they find that personal property taxes and sales taxes have

economically large negative effects on the annual growth of private employment (Mark, et al. 2000).

Harden and Hoyt (2003) point to Phillips and Gross (1995) as another study contending that taxes affect state economic growth, and they assert that the consensus among recent literature is that state and local taxes lower employment. Harden and Hoyt conclude that the corporate income tax has the most significant negative impact on the rate of growth in employment. In addition to affecting the growth rate of employment, the corporate income tax has also been shown to lower the wage rate.[5]

Gupta and Hofmann (2003) regressed capital expenditure against a variety of factors, including weights of apportionment formulas, the number of tax incentives, and burden figures. Their model covered 14 years of data and determined that firms tend to locate property in states where they are subject to income tax factors. Furthermore, Gupta and Hofmann suggest that throwback requirements are most influential on the location of capital investment, followed by apportionment weights and tax rates, and that investment-related incentives have the least impact.

Other economists have found that taxes on specific products can produce behavioral results similar to those that were found in these general studies. For example, Fleenor (1998) looked at the effect of excise tax differentials between states on cross-border shopping and the smuggling of cigarettes. Moody and Warcholik (2004) examined the cross-border effects of beer excises. Their results, supported by the literature in both cases, showed significant cross-border shopping and smuggling between low-tax states and high-tax states.

Fleenor found that shopping areas sprouted in counties of low-tax states that shared a border with a high-tax state, and that approximately 13.3 percent of the cigarettes consumed in the United States during FY 1997 were procured via some type of cross-border activity. Similarly, Moody and Warcholik found that in 2000, 19.9 million cases of beer, on net, moved from low-to-high-tax states. This amounted to some $40 million in sales and excise tax revenue lost in high-tax states.

Even though the general tide of the literature has progressed to the point where the consensus is that taxes are a substantial factor in the decision-making process for businesses, there remain some authors who are not convinced.

Based on a substantial review of the literature on business climates and taxes, Wasylenko (1997) concludes that taxes do not appear to have a substantial effect on economic activity among states. He does, however, cite a *State Policy Report* article that asserts the opposite. As long as the tax elasticity is negative and significantly different from zero, high-tax states will lose more economic activity than average or low-tax states. Indeed, the article goes on to say that the highest-tax states, such as Minnesota, Wisconsin and New York, have acknowledged that high taxes may be responsible for the low rates of job creation in those states.[6]

Wasylenko's rejoinder is that policymakers routinely overestimate the degree to which tax policy affects business location decisions, and that as a result of this misperception, they respond readily to public pressure for jobs and economic growth by proposing lower taxes. According to Wasylenko, other legislative actions are likely to accomplish more positive economic results because in reality, taxes do not drive economic growth. He asserts that lawmakers need better advice than just "Lower your taxes," but there is no coherent message advocating a different course of action.

However, there is evidence that states certainly still compete for businesses using their tax systems. A recent example is that of Intel, an international firm, that was enticed to build a plant in Arizona. From the *San Jose Mercury News*:

> Intel will spend $3 billion to build a next-generation chip factory in Chandler, Arizona. "California has been, in the last 10 to 15 years, pretty expensive," said Chuck Mulloy, an Intel spokesman.[7]

What in fact brought Intel to Arizona was not the type of special package or program targeted at just one firm. Arizona enacted a change in its apportionment formula from a 50 percent sales and 25 percent property and payroll apportionment formula to an 80 percent sales formula.

NEW YORK

New York dropped down to be ranked 49th best this year, leaving only its neighbor New Jersey with a more punishing tax system. New York can blame its fall on the enactment of two new personal income tax brackets this year, with a new top rate of 8.97 percent. That is more than 30 percent higher than its previous top marginal tax rate, and in New York City the additional local rate of 3.648 percent makes the state-local combined rate the highest in the nation.

5 See Robert Carroll, "The Corporate Income Tax and Workers' Wages: New Evidence from the 50 States," *Tax Foundation Special Report*, No. 169 (August 3, 2009), located at http://www.taxfoundation.org/files/sr169.pdf

6 *State Policy Reports*. 1994, Vol. 12, No. 11 (June) , Issue 1 of 2, p.9.

7 Therese Poletti, "Incentive-Rich Arizona to House New Intel Plant," *San Jose Mercury News*, July 26, 2005.

Metrics to Measure the Impact of Tax Differentials

Some recent contributions to the literature on state taxation criticize business and tax climate studies in general. Authors of such studies contend that indexes like the State Business Tax Climate Index do not take into account those factors which directly impact a state's business climate. However, a careful examination of these criticisms reveals that the authors believe taxes are unimportant to businesses and therefore dismiss the studies as merely being designed to advocate low taxes.

Peter Fisher's *Grading Places: What Do the Business Climate Rankings Really Tell Us?*, published by the Economic Policy Institute, criticizes five indexes: The Small Business Survival Index published by the Small Business and Entrepreneurship Council, Beacon Hill's Competitiveness Reports, the Cato Institute's Fiscal Policy Report Card, the Economic Freedom Index by the Pacific Research Institute, and the 2003 edition of this study. Fisher concludes: "The underlying problem with the five indexes, of course, is twofold: none of them actually do a very good job of measuring what it is they claim to measure, and they do not, for the most part, set out to measure the right things to begin with." (Fisher 2005). Fisher's principal argument is that if the indexes did what they purported to do, then all five of them would rank the states similarly.

Fisher's conclusion holds little weight because the five indexes serve such dissimilar purposes and each group has a different area of expertise. There is no reason to believe that the Tax Foundation's Index, which depends entirely on state and local tax laws, would rank the states in the same or similar order as an index that includes crime rates, electricity costs and health care (Small Business and Entrepreneurship Council's Small Business Survival Index), or infant mortality rates and the percentage of adults in the workforce (Beacon Hill's State Competitiveness Report), or charter schools, tort reform and minimum wage laws (Pacific Research Institute's Economic Freedom Index).

The Tax Foundation's State Business Tax Climate Index is an indicator of which states' tax systems are the most hospitable to business and economic growth. The SBTCI does not attempt to measure economic opportunity or freedom, or even the broad business climate, but the narrower business tax climate. We do so not only because the Tax Foundation's expertise is in taxes, but because every component of the SBTCI is subject to immediate change by state lawmakers. It is by no means clear what the best course of action is for state lawmakers who want to thwart crime, for example, either in the short or long term, but they can change their tax codes now. The Tax Foundation believes business decisions are significantly altered by tax considerations, but Fisher takes the contrarian 1970s view that the effects of taxes are "small or non-existent."

Although Fisher does not feel tax climates are important to states' economic growth, other authors contend the opposite. Bittlingmayer, Eathington, Hall and Orazem (2005) find in their analysis of several business climate studies that a state's tax climate does affect its economic growth rate, and that several indexes are able to predict growth. In fact, they found, "The State Business Tax Climate Indexes explains growth consistently." This finding was recently confirmed by Anderson (2006) in a study for the Michigan House of Representatives.

Bittlingmayer, et al., also found that relative tax competitiveness matters, especially at the borders, and therefore, indexes that place a high premium on tax policies better explain growth. Also, they observed that studies focused on a single topic do better at explaining economic growth at borders. Lastly, the article concludes that the most important elements of the business climate are tax and regulatory burdens on business (Bittlingmayer et al. 2005). These findings support the argument that taxes have a significant impact on business decisions and economic growth, and they support the validity of the SBTCI.

Fisher and Bittlingmayer et al. hold opposing views about the impact of taxes on economic growth. Fisher finds support from Robert Tannenwald of the Boston Federal Reserve, who argues that taxes are not as important to businesses as public expenditures. Tannenwald compares 22 states by measuring the after-tax rate of return to cash flow of a new facility built by a representative firm in each state. This very different approach attempts to compute the marginal effective tax rate (METR) of a hypothetical firm and yields results that make taxes appear trivial.

Tannenwald asserts, "While inter-jurisdictional rivalry is inducing states to cut taxes, demand is rising for state and local services such as education, health care, and law enforcement." He concludes that business taxes exert only a small, highly uncertain effect on capital spending. States may be more likely to stimulate their economy by enhancing public services valued by business (Tannenwald 1996).

The taxes paid by businesses should be a concern to everyone because they are ultimately borne by individuals through lower wages, increased prices, and decreased shareholder value. States do not institute tax policy in a vacuum. Every change to a state's tax system makes its business tax climate more or less competitive compared to other states, and makes the state more or less attractive to business. Ultimately, anecdotal and empirical evidence, along with the cohesion of recent literature around the conclusion that taxes matter a great deal to business, show that the SBTCI is an important and useful tool for policymakers who want to make their states' tax systems welcoming to business.

Corporate Tax Index

The first of the five major component indexes that comprise the State Business Tax Climate Index measures the impact of each state's principal tax on business activities. It is well established that the extent of business taxation can affect a business's level of economic activity within a state. For example, Newman (1982) found that differentials in state corporate income taxes were a major factor influencing the movement of industry to southern states. Two decades later, with global investment greatly expanded, Agostini and Tulayasathien (2001) determined that a state's corporate tax rate is the most relevant tax in the investment decisions of foreign investors.

The Corporate Tax Index consists of two distinct, equally weighted sub-indexes—one that measures the impact of the rate structure and one that measures the composition of the business tax base. These two sub-indexes are explained, with notes about which states scored particularly well or poorly on each, and every variable included in the index is described in detail. The final score of the Corporate Tax Index is compiled from these variables and the entire Corporate Tax Index accounts for 20.05 percent of each state's total score. See Tables 8, 9, 10 and 11 in the appendix for details about how every state scores on each variable.

Most states levy standard corporate income taxes. Corporate income is generally defined as profit (gross receipts minus expenses). A growing number of states, however, impose taxes on the gross income of corporations with few or no deductions for expenses. In 2005, for example, Ohio enacted the Commercial Activities Tax (CAT) which taxes gross receipts in excess of $1,000,000 at the rate of 0.26 percent. Washington has the Business and Occupation Tax (B&O) which is a multi-rate tax (depending on industry) on the gross receipts of Washington businesses. Kentucky, New Jersey, and Texas have also recently enacted gross receipts taxes. In 2007, Michigan replaced its Single Business Tax (SBT) with a

Table 2
Major Components of the State Business Tax Climate Index, FY 2010

State	Overall Rank	Corporate Tax Index Rank	Individual Income Tax Index Rank	Sales Tax Index Rank	Unemployment Insurance Tax Index Rank	Property Tax Index Rank
Alabama	19	23	17	25	16	17
Alaska	3	26	1	5	29	15
Arizona	28	22	23	46	2	4
Arkansas	40	39	34	43	17	20
California	48	34	48	48	14	13
Colorado	13	12	16	31	20	6
Connecticut	38	18	24	27	34	48
Delaware	8	49	35	1	13	7
Florida	5	15	1	32	3	22
Georgia	29	8	30	23	22	36
Hawaii	24	10	44	11	12	8
Idaho	18	17	29	12	48	3
Illinois	30	27	10	41	46	39
Indiana	12	21	11	20	11	12
Iowa	46	45	42	33	33	31
Kansas	32	40	21	24	6	32
Kentucky	20	42	32	7	36	19
Louisiana	35	19	25	47	8	24
Maine	34	43	40	6	40	41
Maryland	45	14	49	10	37	38
Massachusetts	36	47	14	26	49	45
Michigan	17	48	15	9	45	33
Minnesota	43	44	37	40	38	16
Mississippi	21	13	18	35	4	23
Missouri	16	5	27	16	7	18
Montana	6	16	22	3	21	10
Nebraska	33	35	31	17	15	34
Nevada	4	3	1	44	42	14
New Hampshire	7	50	9	2	39	40
New Jersey	50	41	47	38	25	50
New Mexico	23	32	19	42	19	1
New York	49	20	50	36	47	43
North Carolina	39	25	36	34	5	37
North Dakota	25	30	33	21	28	5
Ohio	47	38	46	37	10	49
Oklahoma	31	7	26	45	1	27
Oregon	14	31	45	4	30	9
Pennsylvania	27	37	13	29	41	42
Rhode Island	44	36	38	13	50	47
South Carolina	26	9	28	18	43	26
South Dakota	1	1	1	30	35	11
Tennessee	22	11	8	49	32	46
Texas	11	46	7	39	9	30
Utah	10	6	12	28	24	2
Vermont	41	28	41	14	18	44
Virginia	15	4	20	8	44	29
Washington	9	33	1	50	26	21
West Virginia	37	24	39	22	31	28
Wisconsin	42	29	43	19	23	25
Wyoming	2	1	1	15	27	35

Note: Rankings do not average across to total. States without a given tax rank equally as number 1.
Source: Tax Foundation

corporate income tax and a modified gross receipts tax called the Michigan Business Tax (MBT). The MBT taxes gross receipts less the purchases of goods from other firms. Illinois lawmakers also debated a proposal by Governor Blagojevich to swap the state's corporate income tax for a tax on gross receipts, but it was ultimately defeated.

Since gross receipts taxes and corporate income taxes are levied on different bases, we separately compare gross receipts taxes to each other, and corporate income taxes to each other.

For states with corporate income taxes, the state's corporate tax rate sub-index is computed by assessing three key areas: the top tax rate, the level of taxable income at which the top rate kicks in, and the number of brackets. States that levy neither a corporate income tax nor a gross receipts tax clearly achieve a perfectly neutral system in regard to business income and so receive a perfect score.

For states with gross receipts taxes—or their functional equivalent—the state's corporate tax rate sub-index is computed by assessing two key areas: the gross receipts tax rate, and whether the gross receipts rate is an alternative assessment or a generally applicable tax. The latter variable was included so that the states that levy a gross receipts tax as an alternative to the corporate income tax are not unduly penalized.

States that do impose a corporate tax generally will score well if they have a low rate. States with a high rate of or a complex, multiple-rate system score poorly.

To compute the parallel sub-index for the corporate tax base, three broad areas are assessed: tax credits, treatment of net operating losses, and an "other" category that includes variables such as conformity to the Internal Revenue Code, protections against double taxation, and the taxation of "throwback" income provisions, among others. States that score well on the corporate tax base sub-index generally will have few business tax credits, generous carry-back and carry-forward provisions, deductions for net operating losses, conformity to the Internal Revenue Code, and provisions for alleviating double taxation.

Sub-Index #1: Corporate Income Tax Rate

The corporate tax rate sub-index is designed to compare how state corporate income taxes affect competitiveness between states. A state's corporate income tax top rate, income bracket structure, and gross receipts tax rates can affect a business's level of economic activity and the ability of states to attract new businesses.

In addition to the federal corporate income tax, which varies from 15 percent to 35 percent depending on the level of taxable income, states also levy a corporate income tax. Even though the state payment is deductible on the federal return, the combined federal and state top rate is higher than those in all but a few industrial nations. In many states, the combined federal and state corporate tax rates are the highest corporate tax rates in the world.[8]

On the other hand, there are three states (Nevada, South Dakota and Wyoming) that levy neither a corporate income tax nor a gross receipts tax. These states automatically score a perfect 10 for this sub-index. This section ranks the remaining 47 states relative to each other. A discussion of each variable follows.

Top Rate

Graduated Rate Structure

Two variables are used to measure the economic drag or disincentive created by multiple-rate corporate income tax systems. The variables are the income level at which the highest tax rate starts to apply and the number of tax brackets. Thirty-two states and the District of Columbia have a flat, single-rate system, and they score best. Flat rate systems are consistent with the sound principles of simplicity and neutrality. A flat tax system does not impact the economic decisions of businesses as they become more successful and earn additional income.

Top Bracket

This variable measures the income level when a state's tax system applies its highest corporate income tax rate. States score better if their top rate begins at a low income. When the top rate begins at a low level, it performs more like a flat tax. States also score well if their top rate applies only at a very high level of income and only affect a few companies at that rate. States that scored higher because of the high brackets are New Mexico ($1,000,000), Iowa ($250,000), Maine ($250,000) and Vermont ($250,000).[9] States with flat systems also score high since their top rate starts at zero. States where the top begins at

8 Hodge, Scott and Andre Dammert, "U.S. Lags while Competitors Accelerate Corporate Income Tax Reform," *Tax Foundation Fiscal Fact,* No. 184.

9 States whose tax brackets begin at an income threshold that is more than one standard deviation higher than the average threshold receive a perfect score.

medium levels of income scores the worst. Arkansas, Kentucky, Hawaii, and New Jersey all score poorly because their top rates start at $100,000.

Number of Brackets

An income tax system creates changes in behavior when the taxpayer's income reaches the end of one tax rate bracket and moves into a higher bracket. At such a break point, incentives change, and as a result, numerous rate changes are more economically harmful than a single-rate structure. This variable measures the disincentive effect the corporate income tax has on rising incomes. States that score the best on this variable are the 32 states and the District of Columbia that have a single-rate system. Alaska's 10-bracket system earns the worst score in this category. Other states with multi-bracket systems include Arkansas (6 brackets), North Dakota (5 brackets) and Louisiana (5 brackets).

Sub-Index #2: Corporate Income Tax Base

This sub-index measures the economic impact of each state's definition of what should be subject to corporate taxation.

Under a corporate income tax, three criteria used to measure the competitiveness of each state's tax base are given equal weight. The criteria are the availability of certain credits, deductions and exemptions; the ability of taxpayers to deduct net operating losses; and a host of smaller tax base issues that combine to make up the other third of the corporate tax base.

Under a gross receipts tax, these tax base criteria are replaced by the availability of deductions from gross receipts for employee compensation costs and cost of goods sold. States are rewarded for granting these deductions because they diminish the greatest disadvantage of using gross receipts as the base for corporate taxation: the uneven effective tax rates that various industries pay, depending on how many levels of production are hit by the tax.

The three states (Nevada, South Dakota and Wyoming) that levy neither a corporate income tax nor a gross receipts tax, receive a perfect score on both taxes. Missouri, Virginia, Maryland, Hawaii and Oklahoma receive the next best scores. By contrast, New Hampshire has the worst score, preceded by Arkansas, Ohio, Kansas, California, and Washington.

Net Operating Losses

The corporate income tax is designed to tax only the profits of a corporation. However, a yearly profit snapshot may not fully capture a corporation's true profitability. For example, a corporation in a highly cyclical industry may look very profitable during boom years but lose substantial amounts during bust years. When examined over the entire business cycle, the corporation may actually have an average profit margin.

The deduction for net operating losses helps ensure that over time, the corporate income tax is a tax on average profitability. Without the net operating loss deduction, corporations in cyclical industries pay much higher taxes than those paid by stable industries, even assuming identical average profits over time. Put simply, the net operating loss deduction helps level the playing field among cyclical and non-cyclical industries. The federal government currently allows a two-year carry-back cap and a 20-year carry-forward cap. These two variables are taken into account in the index assessment of state tax systems.

OKLAHOMA

Oklahoma's ranking dropped the most this year, from 19th best in 2009 to 31st this year, though not because of new legislative enactments. This year the Tax Foundation was able to obtain much more detailed nationwide data on local-option sales taxes, which turn out to be much higher in Oklahoma than in most states, above 4 percent in several municipalities.

Number of Years Allowed for Carry-Back and Carry-Forward

This variable measures the number of years businesses are allowed to carry-back or carry-forward net operating loss deductions. The longer the over all time span, the higher the probability that the corporate income tax is being levied on the average profitability. In general, states entered 2010 with better treatment of the carry-forward deductions (up to maximum of 20 years) than the carry-back deductions (up to a maximum of three years).

Caps on the Amount of Carry-Back and Carry-Forward

When companies have a higher net operating loss than they can deduct in one year, most states permit them to apply deductions to previous years' returns or to future returns. States that limit such deductions are penalized in the Index. Five states (Delaware, Idaho, New York, Utah, and West Virginia) limit the amount of carry-backs. Only Pennsylvania and New Hampshire limit carry-forwards and as a result, these states score poorly in this variable.

Tax Credits

Many states provide tax credits to lower the effective tax rates for certain industries and/or investments. These are often for large, out-of-state firms considering relocation. Lawmakers create these deals under the banner of job creation and economic development. However, the need for

Table 3
Corporate Tax Index, 2006 – 2010

	FY 2010 Corporate Tax Index		FY 2009 Corporate Tax Index		Change from 2009 to 2010		FY 2008 Corporate Tax Index		FY 2007 Corporate Tax Index		FY 2006 Corporate Tax Index	
State	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank
US	5.00	–	5.00	–	5.00	–	5.00	–	5.00	–	5.00	–
Alabama	5.05	23	5.26	21	–0.20	–2	5.26	21	5.21	21	5.22	22
Alaska	5.02	26	5.03	27	0.00	1	5.03	26	5.00	27	5.01	28
Arizona	5.11	22	5.12	24	0.00	2	5.13	24	5.08	24	5.09	25
Arkansas	4.59	39	4.60	34	0.00	–5	4.60	34	4.56	36	4.57	37
California	4.67	34	4.29	45	0.39	11	4.29	45	4.45	40	4.46	40
Colorado	5.77	12	5.59	15	0.20	3	5.59	16	5.63	15	5.64	15
Connecticut	5.26	18	5.27	18	0.00	0	5.27	18	4.99	28	5.34	18
Delaware	3.66	49	3.77	49	–0.10	0	3.77	48	4.04	48	4.05	47
Florida	5.54	15	5.75	13	–0.20	–2	5.76	14	5.71	14	5.71	14
Georgia	5.92	8	5.93	8	0.00	0	5.94	9	5.99	6	6.00	6
Hawaii	5.79	10	5.81	11	0.00	1	5.81	12	5.86	9	5.87	9
Idaho	5.28	17	5.29	17	0.00	0	5.29	17	5.26	19	5.27	20
Illinois	4.97	27	4.97	28	0.00	1	4.99	28	4.95	30	4.96	30
Indiana	5.18	21	5.18	23	0.00	2	5.20	22	5.16	22	5.17	23
Iowa	4.27	45	4.27	46	0.00	1	4.28	46	4.26	46	4.27	43
Kansas	4.55	40	4.55	37	0.00	–3	4.57	38	4.53	38	4.53	39
Kentucky	4.50	42	4.50	38	0.00	–4	4.51	39	4.39	43	4.89	33
Louisiana	5.25	19	5.25	19	0.00	0	5.27	19	5.33	18	5.33	19
Maine	4.39	43	4.39	43	0.00	0	4.41	43	4.37	44	4.38	42
Maryland	5.58	14	5.58	14	0.00	0	5.98	7	5.93	7	5.94	7
Massachusetts	4.16	47	4.16	47	0.00	0	4.18	47	4.15	47	4.15	45
Michigan	4.03	48	4.03	48	0.00	0	3.29	49	3.47	49	3.47	49
Minnesota	4.32	44	4.32	44	0.00	0	4.34	44	4.31	45	4.23	44
Mississippi	5.62	13	5.82	10	–0.20	–3	5.94	10	5.88	8	5.89	8
Missouri	6.06	5	6.26	5	–0.20	0	6.28	5	5.83	10	5.84	10
Montana	5.42	16	5.42	16	0.00	0	5.64	15	5.59	16	5.60	16
Nebraska	4.67	35	4.67	32	0.00	–3	4.70	31	4.66	34	4.67	35
Nevada	9.44	3	10.00	1	–0.56	–2	10.00	1	10.00	1	10.00	1
New Hampshire	3.29	50	3.29	50	0.00	0	2.99	50	2.88	50	3.56	48
New Jersey	4.55	41	4.47	39	0.08	–2	4.48	40	4.45	41	3.01	50
New Mexico	4.78	32	4.58	35	0.20	3	4.60	35	4.55	37	4.56	38
New York	5.21	20	5.21	22	0.00	2	5.13	23	5.09	23	5.10	24
North Carolina	5.04	25	5.04	26	0.00	1	5.06	25	5.01	25	5.02	26
North Dakota	4.92	30	4.92	30	0.00	0	4.83	30	4.98	29	4.99	29
Ohio	4.60	38	4.63	33	–0.04	–5	4.58	36	4.48	39	4.14	46
Oklahoma	5.95	7	5.95	7	0.00	0	5.97	8	5.72	13	5.73	13
Oregon	4.86	31	5.25	20	–0.39	–11	5.27	20	5.22	20	5.23	21
Pennsylvania	4.62	37	4.42	41	0.20	4	4.43	41	4.40	42	4.41	41
Rhode Island	4.62	36	4.45	40	0.17	4	4.63	33	4.60	35	4.60	36
South Carolina	5.85	9	5.85	9	0.00	0	5.88	11	5.82	11	5.83	11
South Dakota	10.00	1	10.00	1	0.00	0	10.00	1	10.00	1	10.00	1
Tennessee	5.78	11	5.78	12	0.00	1	5.80	13	5.75	12	5.76	12
Texas	4.19	46	4.41	42	–0.23	–4	4.43	42	5.35	17	5.36	17
Utah	6.03	6	6.03	6	0.00	0	6.05	6	6.24	4	6.25	4
Vermont	4.96	28	4.77	31	0.20	3	4.68	32	4.95	31	4.96	31
Virginia	6.32	4	6.32	4	0.00	0	6.34	4	6.18	5	6.79	5
Washington	4.75	33	4.56	36	0.20	3	4.57	37	4.84	33	4.85	34
West Virginia	5.04	24	5.04	25	0.00	1	5.00	27	5.01	26	5.02	27
Wisconsin	4.92	29	4.92	29	0.00	0	4.94	29	4.90	32	4.91	32
Wyoming	10.00	1	10.00	1	0.00	0	10.00	1	10.00	1	10.00	1
District of Columbia	4.58	–	4.58	–	0.00	–	4.59	–	2.18	–	2.19	–

Note: The higher the score, the more favorable a state's tax system is for business. All scores are for fiscal years.
Source: Tax Foundation

states to offer such incentive packages is primarily their bad business tax climates. Tax credits complicate the tax system. They narrow the tax base, drive up tax rates for companies that do not qualify and distort the free market system.

A far more effective approach for improving a state's competitiveness in attracting businesses is to systematically improve the business tax climate for the long term compared to other states. This component index rewards those states that do not offer the following tax credits, and penalizes states that offer them.

Investment Tax Credits

Investment tax credits typically offer an offset against tax liability if the company invests in new property, plants, equipment, or machinery in the state offering the credit. Sometimes, the new investment will have to be "qualified" and approved by the state's economic development office. Such investment tax credits distort the free market by encouraging investment in new property rather than the renovation of old property.

Job Tax Credits

Job tax credits typically offer an offset against tax liability if the company creates a specified number of jobs over a specific time period. Sometimes, the new jobs will have to be "qualified" and approved by the state's economic development office. This is to potentially prevent firms from claiming that jobs were added, when in fact they were merely shifted. Even if administered efficiently, job tax credits can have inefficient outcomes. They cause businesses to hire new employees when their economic position would be best served by spending more on new equipment or marketing. They also reward businesses that are growing and would hire new employees without the credit while penalizing firms that are already struggling to maintain their employment. States that offer job tax credits score poorly on the Index.

Research and Development (R&D) Tax Credits

R&D tax credits reduce the amount of tax due by a company that invests in "qualified" research and development activities. The theoretical argument for R&D tax credits is that it encourages basic research that is not otherwise economically justifiable in the short run but in the long run benefits society. In practice, it greatly complicates the tax systems, and the negative side effects outweigh the potential benefits. Government agencies are often established to assess what types of research qualify and to develop criteria for the tax. States that offer such R&D credits score poorly on the Index.

Gross Receipts Tax Deductions

Proponents of gross receipts taxation invariably claim the steadier flow of tax receipts into government coffers is preferable to the widely fluctuating revenue generated by corporate income taxes. This revenue stability, however, comes at a cost. Firms with many steps in the production process or with high-volume and low margins pay relatively more tax, while vertically-integrated, high-margin firms prosper. Such economic imbalance from this tax often leads lawmakers to enact separate rates for each industry, an inevitably unfair and inefficient process. Two reforms that states can make to mitigate this damage are to permit deductions from gross receipts for employee compensation costs and cost of goods sold, effectively moving toward a regular corporate income tax.

Delaware, Ohio and Washington score the worst for gross receipts tax deductions because they do not offer full deductions for either cost of goods sold or employee compensation. Kentucky and New Hampshire offer deductions for cost of goods sold, Michigan gives a deduction for cost of goods sold and a limited deduction for employee compensation, and Texas gives a deduction for either the cost of goods sold or employee compensation.

Other Significant Features

Federal Income Used as State Tax Base

States that use federal definitions of income help reduce the tax compliance burden on their tax payers.[10] Two states (Arkansas and Mississippi) do not conform to the federal definitions of corporate income. Both are penalized in the Index for this extra burden on businesses.

Allowance of Federal ACRS and MACRS Depreciation

The vast array of federal depreciation schedules is by itself a tax complexity for businesses. The addition of a different state schedule only adds to the complexity. This variable measures the degree to which states have adopted the federal ACRS and MACRS depreciation schedules.[11] Two states that add complexity by failing to fully conform to the federal system are California and Michigan.

10 This is not an endorsement of the economic efficiency of the federal definition of corporate income.

11 This is not an endorsement of the federal ACRS/MACRS depreciation system. It is well known that federal tax depreciation schedules often bear little resemblance to actual economic depreciation rates.

KENTUCKY

Kentucky rose through the ranks faster than any other state this year, up 14 spots from 34th best in the 2009 Index to 20th this year. That might be surprising to Kentuckians who have not seen much change in their tax system, but sometimes standing fast is a virtue. Many economically damaging changes were enacted in other states that previously ranked better than Kentucky. This was particularly true in the personal income tax, where Kentucky saw gains as other states added more brackets with higher rates.

Deductibility of Depletion

The deduction for depletion is similar to the depreciation deduction but applies to the use of natural resources. As with depreciation, tax complexity would be greatly expanded if all 50 states imposed their own depletion schedules. This variable measures the degree to which states have adopted the federal depletion schedules.[12] Eleven states are penalized because they have either adopted their own standards or have just partially conformed to the federal system. Alabama, Minnesota, Oregon, and Wisconsin do not conform at all while Alaska, Delaware, Iowa, Louisiana, New Hampshire, North Carolina and Texas partially conform to the federal schedule.

The Alternative Minimum Tax

The federal Alternative Minimum Tax (AMT) was created to ensure that all taxpayers paid some minimum level of taxes every year. Unfortunately, it creates a parallel tax system to the standard corporate income tax code. Evidence shows that the AMT does not increase efficiency or improve fairness in a meaningful way. It nets little money for the government, imposes compliance costs that in some years are actually larger than collections, and encourages firms to cut back or shift their investments. As such, states have mimicked the federal AMT and put themselves at a competitive disadvantage through needless tax complexity.

Seven states are penalized for enacting a corporate AMT: Alaska, California, Florida, Iowa, Maine, Minnesota and New York.[13]

Deductibility of Taxes Paid

This variable measures the extent of double taxation on income used to pay foreign taxes. This includes paying a tax on money the taxpayer has already mailed to foreign taxing authorities. States can avoid this double taxation by allowing the deduction of taxes paid to foreign jurisdictions. Twenty-one states allow deductions for foreign taxes paid and given a positive score. The remaining 26 states with corporate income taxation do not allow deduction for foreign taxes paid and are penalized.

Indexation of the Tax Code

Some states have brackets that change with nominal increases in income due to inflation. Without inflation adjustments, this "inflation tax" results in higher tax burdens on taxpayers, usually without their knowledge or consent. Fifteen states do not index their corporate income tax brackets. They are Alaska, Arkansas, Hawaii, Iowa, Kansas, Kentucky, Louisiana, Maine, Mississippi, Nebraska, New Jersey, New Mexico, North Dakota, Ohio and Vermont.

Throwback

Most corporations are involved in interstate commerce. To reduce the double taxation of corporate income in the involved states, states use an apportionment system that seeks to determine how much of a company's income it has the right to tax. Generally, states require a company with nexus (that is sufficient connection to the state to justify the state's right to tax its income) to apportion its income to the state based on in-state property, payroll and sales compared to total property, payroll and sales.

Among the 50 states, there is little harmony in apportionment formulas. Many states weight the three factors equally. A recent trend in state tax policy has been to place more weight on sales. Since many businesses make sales into states where they do not have nexus, businesses can end up with income that is not taxed by any state. To counter this phenomenon, many states have adopted what are called throwback rules. Throwback rules identify where the income is derived and throw it back into a state where it will be taxed.

Throwback rules add yet another layer of tax complexity. Since two or more states can theoretically lay claim to this "untaxed" income, rules have to be created and enforced to decide who gets to tax it. States with corporate income taxation are almost evenly divided between those with and without throwback rules. Twenty-three states do not have them, and 24 states and the District of Columbia do.

12 This is not an endorsement of the economic efficiency of the federal depletion system.

13 Five of these states impose both corporate and individual AMTs: California, Iowa, Maine, Minnesota and New York. An individual AMT sub-index is contained within the Individual Income Tax Index.

Individual Income Tax Index

The individual income tax code in each state is also a consideration for business. One important reason is that a significant number of businesses, including sole proprietorships, partnerships and S-corporations, report their income through the individual income tax code. Indeed, the number of individuals filing federal tax returns with business income has nearly doubled over the past 20 years, from 13.3 million in 1980 to 25.5 million in 2002.[14]

Taxes can have a significant impact on an individual's decision to become a self-employed entrepreneur. Gentry and Hubbard (2004) found, "While the level of the marginal tax rate has a negative effect on entrepreneurial entry, the progressivity of the tax also discourages entrepreneurship, and significantly so for some groups of households." (p. 21) Using education as a measure of potential for innovation, Gentry and Hubbard found that a progressive tax system "discourages entry into self-employment for people of all educational backgrounds." Moreover, citing Carroll, Holtz-Eakin, Rider and Rosen (2000), Gentry and Hubbard contend, "Higher tax rates reduce investment, hiring, and small business income growth." (p. 7) Less neutral individual income tax systems, therefore, hurt entrepreneurship and a state's business tax climate.

Another important reason individual income tax rates are critical for business is the cost of labor. Labor typically constitutes a major business expense, so anything that hurts the labor pool will also affect business decisions and the economy. Complex, poorly designed tax systems that extract an inordinate amount of tax revenue are known to reduce both the quantity and quality of the labor pool. This finding was supported by Wasylenko and McGuire (1985), who found that individual income taxes affect businesses indirectly by influencing the location decisions of individuals. A graduated, multi-rate income tax structure exacerbates this problem by systematically ratcheting up the marginal tax rate at higher levels of income. Thus the tax system continually reduces the value of work vis-à-vis the value of leisure.

For example, suppose a worker has to choose between one hour of additional work worth $10 and one hour of leisure which to him is worth $9.50. A rational person would choose to work for another hour. But if a 10-percent income tax rate reduces the after-tax value of labor to $9.00, then a rational person would stop working and take the hour to pursue leisure. Additionally, workers earning higher wages—$30 an hour, for example—that face progressively higher marginal tax rates—20 percent, for instance—are more likely to be discouraged from working additional hours. In this scenario, the worker's after-tax wage is $24 an hour, therefore those workers that value leisure more than $24 an hour will choose not to work. Since the after-tax wage is $6 lower than the pre-tax wage in this example, compared to only $1 lower in the previous example, more workers will choose leisure. In the aggregate, the income tax reduces the available labor supply.

Aside from measuring the economic impact of each state's individual income tax on wage earners, the Individual Income Tax Index measures the impact on non-corporate businesses. Because sole proprietorships, partnerships and S-corporations report business income not on corporate tax returns but on individual tax returns, the structure of the individual income tax code is critical to the business tax climate for these firms.

The individual rate sub-index measures the impact of tax rates on the marginal dollar of individual income using three criteria; the top tax rate, the graduated rate structure, and standard deductions and exemptions, which are treated as a zero percent tax rate. The rates and brackets used are for a single taxpayer, not a couple filing a joint return.

Like the Corporate Tax Index, the Individual Income Tax Index is comprised of two complex sub-indexes measuring the states' tax rate structures and tax bases. Tax rate structure is assessed in four key areas: the states' top marginal tax rates (including local option income rates if a state allows them), the starting points of their top brackets, the number of brackets and the average width of brackets. States that do not impose an individual income tax receive a perfect score, and states that do will generally score well if they have

MILLIONAIRES' TAX

This year a resurgent tax trend spread to several states: enacting disproportionately high tax rates on personal income. Maryland was first in the fall of 2007 when it instituted a new top rate of 6.35 percent on income over $1 million (couples). Since then a number of states have enacted similar taxes, though often on income far less than a million dollars.

The most notable states are Hawaii, New Jersey and Oregon. Hawaii and Oregon now have the highest tax rates in the nation, 11 percent, with Hawaii's kicking in when income exceeds $200,000 and Oregon's when income is greater than $250,000. New Jersey has a top rate of 10.75 percent at an income level of $1 million. Maine also implemented a millionaire's tax of sorts with a last minute political bargain: for income greater than $250,000, the new rate is 6.85 percent while all other income faces a 6.5 percent rate.

14 Scott Hodge and J. Scott Moody, "Wealthy Americans and Business Activity," *Tax Foundation Special Report,* No. 131, August 1, 2004.

a flat, low tax rate with few deductions and exemptions. States that score poorly have complex, multiple-rate systems.

States' tax bases are assessed on a variety of factors, including: how the tax code treats married couples, the lengths to which a tax code goes to

Table 4
Individual Income Tax Index, 2006 – 2010

	FY 2010 Individual Income Tax Index		FY 2009 Individual Income Tax Index		Change from 2009 to 2010		FY 2008 Individual Income Tax Index		FY 2007 Individual Income Tax Index		FY 2006 Individual Income Tax Index	
State	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank
US	5.00	–	5.00	–	5.00	–	5.00	–	5.00	–	5.00	–
Alabama	5.39	17	5.36	17	0.03	0	5.43	17	5.47	17	5.48	17
Alaska	10.00	1	10.00	1	0.00	0	10.00	1	10.00	1	10.00	1
Arizona	5.17	23	5.14	23	0.03	0	5.21	22	5.14	25	5.11	25
Arkansas	4.83	34	4.87	31	–0.04	–3	4.83	34	4.76	33	4.78	32
California	2.68	48	2.15	49	0.53	1	1.93	50	1.99	50	1.99	50
Colorado	6.40	16	6.41	14	–0.01	–2	6.50	14	6.56	14	6.58	14
Connecticut	5.10	24	5.07	25	0.03	1	5.45	16	5.49	16	5.50	16
Delaware	4.80	35	4.95	28	–0.15	–7	4.94	29	4.92	31	4.94	31
Florida	10.00	1	10.00	1	0.00	0	10.00	1	10.00	1	10.00	1
Georgia	4.99	30	4.91	30	0.08	0	4.97	28	5.01	26	5.03	27
Hawaii	3.67	44	4.38	38	–0.71	–6	4.46	37	4.22	42	4.23	42
Idaho	4.99	29	4.86	32	0.13	3	4.93	30	5.01	27	5.03	26
Illinois	6.91	10	6.97	10	–0.06	0	6.82	11	6.85	12	6.87	12
Indiana	6.70	11	6.72	11	–0.02	0	6.88	10	6.85	10	6.97	10
Iowa	3.89	42	3.70	46	0.19	4	3.70	45	3.84	45	4.12	43
Kansas	5.27	21	5.20	21	0.07	0	5.26	20	5.31	20	5.34	20
Kentucky	4.87	32	4.78	36	0.09	4	4.75	35	4.26	41	5.35	41
Louisiana	5.08	25	5.09	24	–0.01	–1	5.13	24	5.18	23	5.20	22
Maine	4.38	40	4.33	40	0.05	0	4.40	39	4.48	37	4.50	38
Maryland	2.52	49	2.06	50	0.46	1	4.42	38	4.54	36	4.55	36
Massachusetts	6.42	14	6.41	16	0.01	2	6.35	15	6.45	15	6.47	15
Michigan	6.41	15	6.41	15	0.00	0	6.61	13	6.74	13	6.77	13
Minnesota	4.45	37	4.34	39	0.11	2	4.39	40	4.47	38	4.50	37
Mississippi	5.38	18	5.35	18	0.03	0	5.41	18	5.44	18	5.46	18
Missouri	5.05	27	4.96	27	0.09	0	4.99	27	4.98	29	4.99	29
Montana	5.25	22	5.15	22	0.10	0	5.19	23	5.26	22	5.28	21
Nebraska	4.93	31	4.85	33	0.08	2	4.91	32	4.61	35	4.63	35
Nevada	10.00	1	10.00	1	0.00	0	10.00	1	10.00	1	10.00	1
New Hampshire	7.43	9	7.55	9	–0.12	0	7.65	9	7.20	9	7.86	8
New Jersey	2.70	47	3.18	48	–0.48	1	2.86	49	2.94	49	3.00	47
New Mexico	5.32	19	5.29	19	0.03	0	5.26	21	5.29	21	5.12	24
New York	2.18	50	4.22	43	–2.04	–7	4.28	42	4.03	44	2.86	49
North Carolina	4.57	36	4.46	37	0.11	1	4.05	44	4.08	43	4.11	44
North Dakota	4.84	33	4.78	35	0.06	2	4.56	36	4.61	34	4.68	34
Ohio	3.39	46	3.22	47	0.17	1	2.98	48	2.94	48	2.96	48
Oklahoma	5.07	26	5.01	26	0.06	0	5.01	26	4.91	32	4.76	33
Oregon	3.43	45	4.84	34	–1.41	–11	4.90	33	4.95	30	4.96	30
Pennsylvania	6.58	13	6.61	12	–0.03	–1	6.69	12	6.91	11	6.93	11
Rhode Island	4.43	38	4.32	42	0.11	4	3.69	46	3.63	47	3.24	46
South Carolina	5.02	28	4.93	29	0.09	1	4.95	31	4.98	28	5.00	28
South Dakota	10.00	1	10.00	1	0.00	0	10.00	1	10.00	1	10.00	1
Tennessee	7.52	8	7.64	8	–0.12	0	7.74	8	7.80	8	7.82	9
Texas	8.59	7	9.44	7	–0.85	0	9.44	7	9.44	7	9.44	7
Utah	6.58	12	6.59	13	–0.01	1	5.11	25	5.17	24	5.19	23
Vermont	3.98	41	3.81	45	0.17	4	3.58	47	3.69	46	3.77	45
Virginia	5.29	20	5.24	20	0.05	0	5.31	19	5.32	19	5.34	19
Washington	10.00	1	10.00	1	0.00	0	10.00	1	10.00	1	10.00	1
West Virginia	4.42	39	4.33	41	0.09	2	4.31	41	4.34	39	4.36	40
Wisconsin	3.70	43	4.21	44	–0.51	1	4.22	43	4.31	40	4.36	39
Wyoming	10.00	1	10.00	1	0.00	0	10.00	1	10.00	1	10.00	1
District of Columbia	4.53	–	4.33	–	0.20	–	4.33	–	4.57	–	4.51	–

Note: The higher the score, the more favorable a state's tax system is for business. All scores are for fiscal years.
Source: Tax Foundation

prevent double taxation, and whether the code is indexed for inflation. States that score well protect married couples from being taxed more severely than if they had filed as two single people. They also protect taxpayers from double taxation by recognizing LLCs and S-corps under the individual tax code and indexing their brackets, exemptions and deductions for inflation.

The income tax also distorts the work and leisure balance. A rational person will work when the benefits from work are greater than the benefits from leisure.

Sub-Index #1: Individual Income Tax Rate

The sub-index compares the 43 states that tax individual income. The seven states that levy no individual income tax receive a perfect score – Alaska, Florida, Nevada, South Dakota, Texas, Washington and Wyoming. Among the other 43, two equally weighted variables are considered to calculate the rate sub-index score: the top tax rate and the graduated rate structure. The states with the top business climate in terms of individual income tax rate are New Hampshire, Tennessee, Illinois, Pennsylvania and Indiana. The worst states were California, New Jersey, Hawaii, Oregon and New York. The factors used to make these judgments will be discussed below.

Top Marginal Tax Rate

California levied the highest statutory income tax rate in the nation last year, but despite a 0.25 percent tax hike, it fell to fifth highest this year. Oregon's 11.36 percent rate is now the highest, combining its new top state-level rate (11 percent) with the weighted average of local rates (0.36 percent). The next four highest income tax rates can be found in Hawaii (11 percent), New Jersey (10.84 percent), New York (10.67 percent) and California (10.55 percent).

Among those states with the lowest top marginal tax rates are New Hampshire (0.85 percent) and Tennessee (1.02 percent).[15] Other states with relatively low top rates include Illinois (3.0 percent of federal AGI), Pennsylvania (4.32 percent), Arizona (4.54 percent), Indiana (4.56 percent of federal AGI), Colorado (4.63 percent of federal taxable income), Connecticut (5 percent) and Mississippi (5 percent).

Graduated Rate Structure

This sub-index measures the impact of a graduated individual income tax structure via three variables: the level of taxable income at which the top rate takes effect, the number of tax brackets and the average width of those brackets. States receive a perfect score if their top rate kicks in at a level of income that is more than one standard deviation higher than the average threshold of all the states.

Top Tax Bracket Threshold

The income level at which a state's top rate kicks in determines the amount of income that is subject to the top rate. States are rewarded for either taxing most income at the top rate (having a low income threshold for the top rate) or taxing very little income at the top rate (having a very high income threshold for the top rate). States whose top rate kicks in at low levels of income effectively have flat rate systems, and states where the kick-in is high have top rates that apply to few taxpayers.

States with flat rate systems score the best on this variable because their top rate kicks in at the first dollar of income after accounting for the standard deduction and personal exemptions. They states include New Hampshire, Tennessee, Pennsylvania, Illinois, Indiana, Michigan and Massachusetts.

Number of Brackets

The Index converts exemptions and standard deductions to a zero bracket before tallying income tax brackets. Therefore, Pennsylvania scores the best in this variable by having only one tax bracket. States with only two brackets are Colorado, Illinois, Indiana, Maine, Massachusetts, Michigan, New Hampshire and Tennessee. On the other end of the spectrum, Hawaii scores the worst in this variable by having twelve tax brackets. Other states with many brackets include Missouri (eleven brackets), Iowa and Ohio (both with ten brackets) and Idaho and Maryland (nine brackets).

The number of brackets listed in a state's tax statutes is not always the number used to calculate the SBTCI. From an economic perspective, standard deductions and exemptions are equivalent to an additional tax bracket with a zero tax rate. As a result, their effects on the income tax have been incorporated into existing sub-indexes.

15 New Hampshire and Tennessee both tax only interest and dividends. To make their top tax rates comparable to together states, the Index calculates the rate needed to collect the same revenue as a typical income tax. Nationally, dividends and interest account for 15.97 percent of income. For New Hampshire, its 5 percent rate was multiplied by 15.97 percent, yielding the equivalent rate of 0.8 percent. For Tennessee, with a tax rate of 6 percent, this calculation yields an equivalent rate of 1.02 percent.

For example, Kansas has a standard deduction of $5,450 and a personal exemption of $2,250 for a combined value of $7,700. Statutorily, Kansas has a top rate on all taxable income over $30,000 and two lower brackets that have an average width of $15,000. But because of its deduction and exemption, Kansas's top rate actually kicks in at $37,700 of income, and it has three tax brackets below that with an average width of $12,567.

The size of allowed standard deductions and exemptions varies considerably.[16]

Connecticut has the largest standard deduction and exemptions ($13,000).[17] Wisconsin has the second highest ($9,490) and a number of states tie for third by conforming to the federal system of $8,950: Colorado, Idaho, Minnesota, New Mexico, North Dakota, Rhode Island, South Carolina and Vermont. On the other hand, Pennsylvania has no standard deduction or personal exemptions, while Indiana and New Jersey allow taxpayers only a $1,000 personal exemption.

The Average Width of Brackets

Many states have several narrow tax brackets close together at the low end of the income scale including a zero bracket created by standard deductions and exemptions. Most taxpayers never notice them because they pass so quickly through those brackets and pay the top rate on most of their income. On the other hand, some states continue placing additional, progressively higher rates throughout the income spectrum, causing individuals and non-corporate businesses to alter their income-earning and tax-planning behavior. This sub-index punishes the latter group of states by measuring the average width of the brackets, rewarding those states where the average width is small, with the result that the top rate is levied on most income, acting effectively as a flat rate on all income.

CALIFORNIA

With such a low ranking, it may not assuage California taxpayers to hear that the state's tax system has improved one spot this year and now ranks 48th best. Unfortunately, even this slightly good news does not come because of improved tax policy. New York implemented even worse policies, dropping below California. In fact, California's raw score dropped substantially because it added 0.25 percent to each personal income tax rate and increased its statewide sales tax to 8.25 percent, now the nation's highest state-level rate.

The state that scores the best is Pennsylvania, since it has no separate brackets. Indiana comes in second with an average width of $1,000. Other states with similar bracket structures include Missouri ($1,655), Oklahoma ($1,850), and Georgia and Illinois ($2,000). California scores the worst with an average bracket width of $143,561. Other low-scoring states include Maryland ($125,650), New Jersey ($83,500) and Vermont, Rhode Island and North Dakota ($71,730).

Sub-Index #2: The Individual Income Tax Base

States have different definitions of taxable income, and some create greater impediments to economic activity. This sub-index gives equal weight to the three components. Marriage penalty and double taxation of capital income are two components and the third addresses a number of minor tax base issues.

The seven states with no individual income tax of any kind achieve perfect neutrality. Texas, however, receives a slight deduction because it does not recognize LLCs or S-Corps. Of the other 43 states, Utah, Idaho, Oregon, Indiana, Tennessee, Montana and West Virginia have the highest scores. They avoid the marriage penalty and have other problems with the definition of taxable income. States where the tax base is found to cause an unnecessary drag on economic activity are Maryland, California, New Jersey, Rhode Island, Ohio and West Virginia.

Marriage Penalty

A marriage penalty exists when a state's standard deduction and tax brackets for married taxpayers filing jointly are not double those for single filers. As a result, two singles (if combined) can have a lower tax bill than a married couple filing jointly with the same income. This is discriminatory and has serious business ramifications. Eighty-five percent of the top-earning 20 percent of taxpayers are married couples. This same 20 percent also has the highest concentration of business owners (43 percent) of all income groups (Hodge 2003A, Hodge 2003B). Because of these concentrations, marriage penalties affect a large majority of taxable income. States with the largest marriage penalties include Maryland, California, New Jersey, Ohio, Rhode Island, Vermont and North Dakota.

Many states get around the marriage penalty problem by allowing married couples to file as if they were singles. While helpful in offsetting the marriage penalty, it comes at the expense of added

16 Some states offer tax credits in lieu of income exemptions. Rather than excluding a portion of a taxpayer's income form the income tax, tax credits, reduce a taxpayer's tax liability. The result is the same: a lower income tax bill. In order to maintain consistency within the sub-index, a tax credit is converted to an equivalent income exemption.

17 In Connecticut, taxpayers receive a declining exemption and a personal tax credit. The exemption starts at $13,000 and phases out after $55,000 of income for single taxpayers.

tax complexity. Despite the complexity, the sub-index rewards states that have this provision.

Double Taxation of Capital Income

Since several states with an individual income tax system mimic the federal income tax code, they

Table 5
Sales Tax Index, 2006 – 2010

State	FY 2010 Sales Tax Index Score	FY 2010 Sales Tax Index Rank	FY 2009 Sales Tax Index Score	FY 2009 Sales Tax Index Rank	Change from 2009 to 2010 Score	Change from 2009 to 2010 Rank	FY 2008 Sales Tax Index Score	FY 2008 Sales Tax Index Rank	FY 2007 Sales Tax Index Score	FY 2007 Sales Tax Index Rank	FY 2006 Sales Tax Index Score	FY 2006 Sales Tax Index Rank
US	5.00	–	5.00	–	5.00	–	5.00	–	5.00	–	5.00	–
Alabama	4.57	25	4.01	34	0.56	9	4.01	34	4.27	27	5.28	21
Alaska	8.12	5	8.29	5	–0.17	0	8.29	5	7.93	5	9.63	1
Arizona	3.21	46	3.30	46	–0.09	0	3.30	46	3.32	47	4.49	42
Arkansas	3.53	43	3.83	38	–0.30	–5	3.83	38	3.67	39	4.67	39
California	2.81	48	3.45	44	–0.64	–4	3.45	44	3.47	44	4.68	38
Colorado	4.27	31	5.67	10	–1.40	–21	5.67	10	6.00	7	5.12	24
Connecticut	4.51	27	4.29	29	0.22	2	4.29	29	4.04	34	4.83	34
Delaware	9.30	1	9.49	2	–0.19	1	9.49	2	9.56	2	9.53	3
Florida	4.22	32	4.40	24	–0.18	–8	4.40	24	4.62	21	5.41	18
Georgia	4.61	23	4.59	19	0.01	–4	4.59	19	4.70	19	6.33	6
Hawaii	5.27	11	5.28	11	–0.01	0	5.28	11	5.52	12	5.11	25
Idaho	5.22	12	4.97	15	0.25	3	4.97	15	4.82	17	4.76	35
Illinois	3.60	41	3.94	36	–0.33	-5	3.94	36	4.00	36	5.09	26
Indiana	4.66	20	4.51	22	0.16	2	4.51	22	5.07	15	5.81	13
Iowa	4.16	33	4.24	30	–0.09	-3	4.24	30	4.52	22	5.38	19
Kansas	4.58	24	4.54	20	0.04	–4	4.54	20	4.30	26	4.97	32
Kentucky	6.25	7	6.14	6	0.11	–1	6.14	6	6.01	6	5.88	10
Louisiana	3.13	47	3.23	47	–0.11	0	3.23	47	3.24	48	4.01	45
Maine	6.43	6	6.10	7	0.34	1	6.10	7	5.89	8	5.72	14
Maryland	5.27	10	5.06	13	0.21	3	5.06	13	5.58	11	6.08	8
Massachusetts	4.53	26	5.13	12	–0.60	–14	5.13	12	5.32	13	5.86	12
Michigan	6.13	9	5.90	9	0.23	0	5.90	9	5.70	10	5.68	15
Minnesota	3.62	40	3.70	42	–0.08	2	3.70	42	3.61	42	4.60	40
Mississippi	4.05	35	3.94	35	0.10	0	3.94	35	3.83	37	4.68	37
Missouri	4.93	16	4.36	26	0.57	10	4.36	26	4.41	24	5.87	11
Montana	9.10	3	9.30	3	–0.21	0	9.30	3	9.28	3	9.21	5
Nebraska	4.87	17	4.39	25	0.48	8	4.39	25	4.15	31	4.36	44
Nevada	3.43	44	3.32	45	0.11	1	3.32	45	3.36	45	3.36	49
New Hampshire	9.30	2	9.58	1	–0.29	–1	9.58	1	9.57	1	9.61	2
New Jersey	3.79	38	3.62	43	0.17	5	3.62	43	3.35	46	5.04	29
New Mexico	3.56	42	3.21	48	0.36	6	3.21	48	3.49	43	3.96	46
New York	4.02	36	3.86	37	0.16	1	3.86	37	4.09	32	3.48	48
North Carolina	4.14	34	3.75	41	0.39	7	3.75	41	3.63	41	4.51	41
North Dakota	4.64	21	4.22	31	0.42	10	4.22	31	4.07	33	5.28	22
Ohio	3.94	37	3.79	39	0.15	2	3.79	39	3.76	38	4.45	43
Oklahoma	3.27	45	4.14	33	–0.87	–12	4.14	33	4.03	35	5.01	30
Oregon	9.04	4	9.28	4	–0.24	0	9.28	4	9.27	4	9.24	4
Pennsylvania	4.42	29	4.30	28	0.12	–1	4.30	28	4.27	28	5.09	27
Rhode Island	5.14	13	5.03	14	0.11	1	5.03	14	4.86	16	4.74	36
South Carolina	4.76	18	4.73	16	0.03	–2	4.73	16	4.63	20	5.91	9
South Dakota	4.33	30	3.77	40	0.57	10	3.77	40	3.64	40	4.97	31
Tennessee	2.60	49	2.67	49	–0.07	0	2.67	49	2.59	49	3.49	47
Texas	3.74	39	4.17	32	–0.44	–7	4.17	32	4.17	30	4.92	33
Utah	4.47	28	4.32	27	0.15	–1	4.32	27	4.18	29	5.20	23
Vermont	5.03	14	4.66	18	0.37	4	4.66	18	4.81	18	5.54	16
Virginia	6.14	8	5.96	8	0.19	0	5.96	8	5.76	9	6.30	7
Washington	2.11	50	2.02	50	0.09	0	2.02	50	2.05	50	3.25	50
West Virginia	4.63	22	4.45	23	0.18	1	4.45	23	4.50	23	5.31	20
Wisconsin	4.69	19	4.53	21	0.16	2	4.53	21	4.35	25	5.09	28
Wyoming	4.99	15	4.73	17	0.26	2	4.73	17	5.32	14	5.43	17
District of Columbia	4.76	–	4.63		0.12	–	4.63	–	4.45	–	4.22	–

Note: The higher the score the better, the more favorable a state's tax system is for business. All scores are for fiscal years.
Source: Tax Foundation

also possess its greatest flaw, the double-taxation of capital income. Double taxation is brought about by the interaction between the corporate income tax and the individual income tax. The ultimate source of most capital income—interest, dividends and capital goods—is corporate profits. The corporate income tax reduces the level of profits that can eventually be used to generate interest or dividend payments or capital gains. This capital income must then be declared by the receiving individual and taxed. The result is the double taxation of this capital income, first at the corporate level and again on the individual level.

All states with an individual income tax score poorly by this criterion except Tennessee and New Hampshire. These states tax individuals on interest and dividends, but not capital gains.

Other Significant Issues

The index includes several individual income tax base issues that significantly affect the neutrality of state individual income tax systems.

Federal Income Used as State Tax Base

Despite the shortcoming of the federal government's definition of income, states that use it help reduce the tax compliance burden on taxpayers. Eight states do not conform to federal definitions of individual income: Alabama, Arkansas, Iowa, Mississippi, New Hampshire, New Jersey, Pennsylvania and Tennessee. These states are penalized for the complexity they induce with alternative income definitions.

The Alternative Minimum Tax

The Alternative Minimum Tax (AMT) was created at the federal level in 1969 to ensure that all taxpayers paid some minimum level of taxes every year. Unfortunately, it creates a parallel tax system to the standard individual income tax code. Evidence shows that the AMT is an inefficient way to prevent tax deductions and credits from totally eliminating tax liability. As such, states that have mimicked the federal AMT put themselves at a competitive disadvantage by adding complexity.

Twelve states have an AMT on individual income: California, Colorado, Connecticut, Iowa, Maine, Maryland, Minnesota, Nebraska, New York, Rhode Island, West Virginia and Wisconsin. These states are penalized accordingly.

Deductibility of Taxes Paid

This variable measures the extent of double taxation on income used to pay foreign and state taxes, i.e., paying a tax on a tax. States can avoid double taxation by allowing a deduction for state taxes paid to other jurisdictions.

Recognition of Limited Liability Corporation and S-Corporation Status

One important development in the federal tax system is the creation of the limited liability corporation (LLC) and the S-corporation (S-corp). LLCs and S-corps provide businesses some of the benefits of incorporation, such as limited liability, without the overhead of becoming a regular C-corporation. They also are taxed as individuals, which avoids the double-taxation problems that plague the corporate income system. Every state with a full individual income tax recognizes LLCs or S-corporations to at least some degree.

Indexing of the Tax Code

Indexing the tax code for inflation is critical in order to prevent de facto tax increases on the nominal increase in income due to inflation. Put simply, this "inflation tax" results in higher tax burdens on taxpayers, usually without their knowledge or consent. Three areas of the individual income tax are commonly indexed for inflation: the standard deduction, personal exemptions and tax brackets.

Sales Tax Index

The type of sales tax familiar to all taxpayers is a tax levied on the purchase price of a good or service at the point of sale. This point-of-sale tax can hurt the business tax climate because as the sales tax rate climbs, customers either make fewer purchases or seek out low-tax alternatives. As a result, business is reduced generally or lost to lower-tax locations, causing lost profits, lost jobs and lost tax revenue.[18] The effect of differential sales tax rates between states or localities is apparent when a traveler crosses the state line from a high-tax state to a neighboring low-tax state. Typically, a vast expanse of shopping malls has sprung up along the border in the low-tax jurisdiction.

18 States try to limit sales tax competition by levying a use tax on good purchased out of state and brought into the state. Enforcement of use tax obligations against consumers is nearly impossible, especially after the Supreme Court's decision in *Quill v. Heitkamp,* 504 U.S. 298 (1992), where the Court ruled that vendors without physical presence (offices, employees, etc.) in a state could not be forced to collect use tax. The Streamlined Sales Tax Project is a current effort of state revenue commissioners and multistate businesses to harmonize state sales and US tax bases such that Congress could be justified in overturning the *Quill* decision.

On the positive side, sales taxes levied on goods and services at the point of sale to the end user have at least two virtues. They are "transparent," i.e., the tax is never confused with the price of goods by customers, and since they are levied at the point of sale, they are less likely to cause economic distortions than taxes levied at some intermediate stage of production.

More detrimental to the business climate are sales taxes levied on business-to-business transactions. When a business must pay sales taxes on manufacturing equipment and raw materials, then that tax becomes part of the price of whatever the business makes with that equipment and those materials. Of course, it must then collect sales tax on its own products, with the result that a tax is being charged on a tax. So-called "tax pyramiding" invariably results in some industries being taxed more heavily than others, which causes economic distortions.

Consider the following quote from David Brunori, contributing editor of *State Tax Notes:*

> A graduate student wrote me recently and asked what I thought was the most egregious flaw embedded in the state tax system. I told her that I thought there were about 100 flaws that could vie for the top spot. Here is one: the sales tax on business purchases. Everyone who has ever studied the issue will tell you that the sales tax should not be imposed on business purchases. That is, when a business purchases a product or service, it should not pay tax on the purchase. There is near unanimity among public finance scholars on the issue. The sales tax is supposed to be imposed on the final consumer. Taxing business purchases causes the tax to be passed on to consumers without their knowledge. There is nothing efficient or fair about that. But business purchases are taxed widely in every state with a sales tax. Some studies have estimated that business taxes make up nearly 50 percent of total sales tax revenue. Why? Two reasons. First, because business sales taxes raise so much money that the states cannot repeal them. The states would have to either raise other taxes or cut services. Second, many politicians think it is only fair that "businesses" pay taxes because individuals pay them. That ridiculous belief is unfortunately shared by many state legislators; it's usually espoused by liberals who don't understand that businesses aren't the ones who pay taxes. People do. Every time a business pays sales tax on a purchase, people are burdened. They just don't know it.[19]

The negative impact of sales taxes is well documented in the economic literature and through anecdotal evidence. For example, Bartik (1989) found that high sales taxes, especially sales taxes levied on equipment, had a negative effect on small business start-ups. Moreover, companies have been known to avoid locating factories or facilities in certain states because the factory's machinery would be subject to the state's sales tax.[20]

To understand how business-to-business sales taxes can distort the market, suppose a sales tax were levied on the sale of flour to a bakery. The bakery is not the end-user because the flour will be baked into bread and sold to consumers. Economic theory is not clear as to which party will ultimately bear the burden of the tax. The tax could be "passed forward" onto the customer or "passed backward" onto the bakery.[21] Where the tax burden falls depends on how sensitive the demand for bread is to price changes. If customers tend not to change their bread-buying habits when the price rises, then the tax can be fully passed forward onto consumers. However, if the consumer reacts to higher prices by buying less, then the tax will have to be absorbed by the bakery as an added cost of doing business.

The hypothetical sales tax on all flour sales would distort the market because different businesses that use flour have customers with varying price sensitivity. Suppose the bakery is able to pass the entire tax on flour forward to the consumer, but the pizza shop down the street cannot. The owners of the pizza shop would face a higher cost structure and profits would drop. Since profits are the market signal for opportunity, the tax would tilt the market away from pizza-making. Fewer entrepreneurs would enter the pizza business, and existing businesses would hire

ILLINOIS

Illinois saw a drop in their overall rank this year but prevented a further slide when the legislature declined to pass a 50-percent increase in the income tax proposed by the Governor Quinn. Alternatively, the state increased several excise taxes, which hurt the state's score somewhat. The dubious distinction of having the highest combined state-local sales tax goes to Bellwood, Illinois, a village to the west of Chicago. Individuals making purchases in Bellwood's business district owe 6.25 percent to the state, 2.75 percent to Cook County, and finally 1.5 percent to Bellwood Village, a combined total of 10.5 percent.

19 David Brunori, "An Odd Admission of Gambling," State Tax Notes, Jan. 30, 2005, pp. 332 – 339.

20 In early 1993, Intel Corporation was considering California, New Mexico and four other states as the site of a new billion dollar factory. California was the only one of the six states the levied its sales tax on machinery and equipment, a tax that would have cost Intel roughly $80 million. As Intel's Bob Perlman put it in testimony before a committee of the California state legislature, "There are two ways California's not going to get the $80 million, with the factory or without it." California would not repeal the tax on machinery and equipment; New Mexico got the plant.

21 Besley and Rosen

fewer people. In both cases, the sales tax charged to purchasers of bread and pizza would be partly a tax on a tax because the tax on flour would be built into the price. Economists call this tax pyramiding.

Besley and Rosen (1998) found that for many products, the after-tax price of the good increased by the same amount as the tax itself. That means a sales tax increase was passed along to consumers on a one-for-one basis. For other goods, however, they found that the price of the good rose by twice the amount of the tax, meaning that the tax increase translates into an even larger burden for consumers than is typically thought.

CIGARETTE TAXES

Cigarettes were in the crosshairs of a large number of state legislatures this year. Ten states enacted cigarette tax increases this year: Arkansas, Florida, Hawaii, Kentucky, Mississippi, New Jersey, New Hampshire, Rhode Island, Vermont and Wisconsin. Florida and Rhode Island raised their rates by the most, a dollar per pack. In percentage terms, Florida's tax hike was the largest: 300%. The highest rate state rate remains with Rhode Island at $3.46, and the lowest rate is still in South Carolina at $0.07. These rates do not take into consideration the local cigarette taxes. New York City has a combined rate of $4.25.

The logistics of the Sales Tax Index are as follows. The weight of the Sales Tax Index is 24.14 percent thus making up nearly a quarter of the entire index's score. Like the other component indexes, this is made of two equally weighted sub-indexes: the sales tax rate index and the sales tax base. The rate sub-index is calculated using two criteria: the state-level rate and the combined state-local rate. States will score well if they either do without a sales tax or if the combined state and local sales tax rate is low. The ideal base for sales tax is that all goods and services are taxed at the point of sale to the end user.

There are five states without a state sales tax: Alaska, Delaware, New Hampshire, Oregon and Montana. For this they receive the highest score on the index.

Sub-Index #1: Sales Tax Rate

The tax rate is an important and transparent measure of the tax climate. A disproportionally high rate will reduce the quantity demanded for in-state retail sales. This will lead consumers to seek goods through other sources such as catalog and internet sales and results in less business activity in the state.

The State Business Tax Climate Index measures the state and local sales tax rate in each state. A combined rate is computed by summing the state sales tax rate and the weighted average of the county and municipal rates.

State-Level Sales Tax Rate

Disregarding the states that do not charge a state sales tax, Colorado has the lowest state-wide sales tax of 2.90 percent. Seven states have a state tax rate of 4 percent: Alabama, Georgia, Hawaii, Louisiana, New York, South Dakota and Wyoming.[22]

On the other end of the spectrum, the highest state-level sales tax is California's at 8.25 percent. This is followed by a 7 percent rate in 5 states: Indiana, Mississippi, New Jersey, Rhode Island and Tennessee. In last years Index, Tennessee was the only state with a 7 percent sales tax.

Local Option Sales Tax Rates

Comparisons of state-level sales taxes miss an entire layer of taxation beneath it in many states. Thirty-two states have some level of local option sales tax. Because there are so many localities, the Index calculates a weighted average rate for each state. This is done by weighting each 5 digit zip code's rate by percentage of total state personal income.

Despite the difficulties associated with this mass of local data, it is essential to include the local option sales tax to portray an accurate picture of the actual sales tax paid. For example, Louisiana has what looks like a low sales tax with a state-level rate of 4 percent. The local sales tax rate, however, eclipses the state rate. Averaging 4.46 percent, it brings the total sales tax paid to an average of 8.46 percent. It is rare for the local tax rate to be higher than the state's, but in a number of states the local option sales tax significantly increases the tax rate paid by consumers.

There are currently three states that charge over a 4 percent local rate: Louisiana (4.46 percent), New York (4.25 percent) and Colorado (4.21 percent), and Oklahoma's rate is close (3.92 percent). Eight states have an average local sales tax rate between 2 and 3 percent.

The sub-index sums the state and local taxes together and grades states on the combined rate. States with the highest combined rates are Tennessee (9.42 percent), California (9.06 percent), Washington (8.65 percent), Louisiana (8.46 percent), and Oklahoma (8.42 percent). At the bottom end, aside from the states with no sales tax, are Alaska (0.86 percent)[23], Hawaii (4.35 percent), Maine (5.00 percent), Virginia (5.00 percent), and Wyoming (5.37 percent).

22 Virginia has a 4% state rate and a state-mandated 1% "local" rate collected by the state government.

23 Alaska has no state-level sales tax, but it does allow local option sales taxes. For example, Juneau has a 5 percent local option sales tax.

Local Option Sales Tax Base

In addition to the distortions created when states allow localities to tax at different rates, a large number of states allow local jurisdictions to define the tax base.

Sub-Index #2 Sales Tax Base

The Sale Tax Base sub-index is further broken down to look at three categories, 1) business-to-business transactions, 2) consumer goods and services base, and 3) excise tax rate for specific products.

The top five states on this sub-index are those without a general state-level sales tax – Alaska, Delaware, Montana, New Hampshire and Oregon. This does not mean that they receive perfect scores, however, due to the fact that all states levy some form of excise tax on gasoline, diesel, tobacco, and beer. For the states that do have a general sales tax, Missouri, South Carolina, Kentucky, Virginia, and Maryland score the best. To score high, these states avoid excessively high excise taxes and problems associated with tax pyramiding.

The states that score the worst do so because they tax business-to-business transactions, narrow the base for consumer products and have higher rates on excise taxes. The states that did the worst were Hawaii, New Mexico, South Dakota, Washington and Nebraska.

Business Inputs

These variables are often inputs to other business operations. For example, a manufacturing firm will count the cost of transporting its final goods to retailers as a significant cost of doing business. Most firms, small and large alike, hire accountants, lawyers, and other professional service firms. If these services are taxed, then it is more expensive for every business to operate.

Note that these inputs should only be exempt for sales tax if they are truly inputs into the production process. If they are consumed by an end user, they are properly includable in the state's sales tax base.

Agricultural Inputs

- Insecticides and pesticides
- Fertilizer, seed and feed
- Seedlings, plants and shoots

Service Inputs

- Cleaning services
- Transportation services
- Repair services
- Professional/personal services
- General treatment

Manufacturing and Machinery Inputs

- Manufacturing machinery
- Utilities
- Farm machinery
- Raw materials
- Office equipment

Computer and Software Inputs

- Custom software
- Modified canned software
- Downloaded software

Leasing and Rental Inputs

- Motor vehicles
- Rooms and lodging
- All other tangible personal property

Pollution Control Equipment

- Air pollution control equipment
- Water pollution control equipment

Consumer Goods and Services

A state sales tax base should include all goods and services purchased by the end users of those products. Exempting any goods or services narrows the tax base, drives up the sales tax rate and introduces unnecessary distortion into the market.

Gasoline

Purchases of gasoline should be included in the sales tax base, even though every state subjects gasoline to a separate excise levy at the distributor stage of production. Ideally, the excise tax can be viewed as a user fee that funds road construction, and where this is the case, no damaging tax pyramiding is caused by levying both an excise and a general sales tax on gasoline. There is no economic reason to exclude gasoline from the sales tax base since the sales tax is intended to apply broadly to all consumption. Thus, the Index gives a better score to states that include gasoline in the sales tax base.

Four states fully include gasoline in their sales tax base: California, Illinois, Indiana and Michigan. Connecticut, Georgia and New York get partial credit for applying an ad valorem tax to gasoline sales, but at a different rate than for the general sales tax.

Groceries

A principled approach to tax policy calls for all end-user goods to be included in the tax base, to keep the base broad, rates low, and prevent distortions in the marketplace. Should groceries be the exception?

Many state officials will say that they exempt groceries in order to make the sales tax system

Table 6
Property Tax Index, 2006 – 2010

State	FY 2010 Property Tax Index		FY 2009 Property Tax Index		Change from 2009 to 2010		FY 2008 Property Tax Index		FY 2007 Property Tax Index		FY 2006 Property Tax Index	
	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank
US	5.00	–	5.00	–	5.00	–	5.00	–	5.00	–	5.00	–
Alabama	5.72	17	5.83	13	–0.11	–4	5.83	13	5.60	16	6.34	7
Alaska	5.84	15	5.11	27	0.73	12	5.25	21	5.54	18	5.48	19
Arizona	6.45	4	6.41	4	0.04	0	6.48	5	6.21	7	6.25	8
Arkansas	5.38	20	5.45	18	–0.07	–2	5.68	17	5.95	11	6.09	11
California	5.86	13	5.82	15	0.04	2	5.77	15	5.59	17	5.67	16
Colorado	6.34	6	6.28	6	0.06	0	6.29	7	6.06	9	6.13	10
Connecticut	3.61	48	3.05	49	0.56	1	3.04	50	2.81	49	2.12	50
Delaware	6.26	7	6.16	8	0.10	1	6.19	8	6.31	5	6.48	5
Florida	5.31	22	5.44	19	–0.13	–3	5.58	19	4.79	31	4.76	29
Georgia	4.38	36	4.31	36	0.07	0	4.41	35	5.22	23	5.26	22
Hawaii	6.13	8	6.14	9	–0.01	1	6.54	4	6.29	6	6.42	6
Idaho	6.50	3	6.50	3	0.00	0	6.81	2	6.83	3	6.90	3
Illinois	4.10	39	4.02	41	0.08	2	3.91	40	4.19	39	4.13	38
Indiana	5.87	12	6.27	7	–0.40	–5	5.66	18	4.88	29	4.90	28
Iowa	4.59	31	4.48	33	0.10	2	4.43	34	4.73	33	4.70	31
Kansas	4.56	32	4.54	32	0.02	0	4.32	36	4.63	34	4.60	33
Kentucky	5.39	19	5.43	20	–0.04	1	5.38	20	5.70	13	4.65	32
Louisiana	5.21	24	5.20	22	0.01	–2	4.75	30	5.08	25	5.22	23
Maine	3.97	41	4.07	40	–0.10	–1	3.85	41	4.22	38	4.07	39
Maryland	4.22	38	4.38	34	–0.16	–4	4.11	39	3.84	41	3.87	40
Massachusetts	3.65	45	3.59	44	0.07	–1	3.57	44	3.70	43	3.67	43
Michigan	4.54	33	5.16	25	–0.62	–8	5.15	24	4.52	35	4.94	26
Minnesota	5.82	16	5.79	17	0.03	1	5.95	11	5.65	15	5.70	15
Mississippi	5.31	23	4.89	29	0.42	6	4.95	29	5.29	21	5.36	21
Missouri	5.47	18	6.02	11	–0.55	–7	6.01	10	5.84	12	5.95	13
Montana	5.95	10	6.03	10	–0.08	0	6.02	9	5.18	24	5.12	24
Nebraska	4.53	34	3.38	48	1.15	14	3.31	48	3.52	45	3.45	46
Nevada	5.86	14	5.79	16	0.07	2	5.83	14	5.65	14	5.71	14
New Hampshire	4.08	40	4.10	39	–0.02	–1	4.48	32	4.74	32	4.33	37
New Jersey	2.86	50	2.90	50	–0.04	0	3.17	49	3.34	46	3.16	47
New Mexico	7.12	1	7.16	1	–0.04	0	7.13	1	7.50	1	7.69	1
New York	3.86	43	3.57	45	0.28	2	3.76	42	3.73	42	3.60	45
North Carolina	4.23	37	4.15	37	0.08	0	4.14	37	3.85	40	3.70	42
North Dakota	6.43	5	6.29	5	0.13	0	6.27	6	6.62	4	6.67	4
Ohio	3.57	49	3.55	46	0.02	–3	3.60	43	3.16	47	3.12	48
Oklahoma	5.08	27	5.19	23	–0.11	–4	5.16	23	5.42	20	5.56	18
Oregon	5.97	9	5.83	14	0.13	5	5.72	16	6.03	10	6.07	12
Pennsylvania	3.88	42	3.41	47	0.47	5	3.45	46	3.70	44	3.66	44
Rhode Island	3.61	47	3.72	43	–0.11	–4	3.35	47	2.70	50	2.54	49
South Carolina	5.10	26	5.12	26	–0.02	0	5.09	27	4.91	28	4.93	27
South Dakota	5.94	11	5.85	12	0.09	1	5.84	12	6.10	8	6.18	9
Tennessee	3.62	46	4.15	38	–0.53	–8	4.14	38	4.40	37	4.50	34
Texas	4.90	30	4.71	30	0.19	0	4.61	31	4.49	36	4.43	36
Utah	6.76	2	6.64	2	0.12	0	6.66	3	7.00	2	7.10	2
Vermont	3.78	44	3.73	42	0.05	–2	3.49	45	3.06	48	3.76	41
Virginia	5.04	29	4.99	28	0.05	–1	5.19	22	4.97	26	4.43	35
Washington	5.32	21	5.24	21	0.08	0	5.12	26	4.91	27	4.96	25
West Virginia	5.06	28	5.19	24	–0.13	–4	5.13	25	5.46	19	5.56	17
Wisconsin	5.14	25	4.58	31	0.55	6	4.47	33	4.81	30	4.73	30
Wyoming	4.45	35	4.35	35	0.10	0	5.00	28	5.28	22	5.37	20
District of Columbia	4.95	–	4.29	–	0.66	–	4.09	–	4.36	–	4.53	–

Note: The higher the score, the more favorable a state's tax system is for business. All scores are for fiscal years.
Source: Tax Foundation

easier on low-income persons. In reality, exempting groceries from the sales tax mostly benefits grocers, not the poor, although even grocers have occasion to complain because the maintenance of complex, ever changing lists of exempt and non-exempt products constitutes an administrative burden for all concerned. Most importantly, though, widespread availability of public assistance for the purchase of groceries—through the Women, Infants and Children program or the food-stamp program—makes the argument for such exemptions unpersuasive.

Excise Taxes

Excise taxes are single-product sales taxes. Many of them are intended to reduce consumption of the product bearing the tax. Others, like the gasoline tax, are often used to fund specific projects like road construction. The sub-index tallies:

- Gasoline excise tax
- Diesel excise tax
- Tobacco excise tax
- Beer excise tax
- Spirits excise tax

Gasoline and diesel excise taxes (levied on a per gallon basis) are usually levied on the benefit principle as a means to pay for road construction and maintenance. Since gasoline represents a large input for most businesses, states that levy higher rates have a less competitive business tax climate. States with the highest gasoline taxes are Washington (37.5 cents), Florida (33.2 cents), New York (33.2 cents), Wisconsin (32.9 cents) and Nevada (32.6 cents).

States with the highest tobacco taxes per pack of 20 cigarettes are Rhode Island ($3.46), New York ($2.75), New Jersey ($2.70), Hawaii ($2.60) and Wisconsin ($2.52). States with the lowest tax on cigarettes are South Carolina ($0.07), Missouri ($0.17), Virginia ($0.30), North Carolina ($0.35) and Louisiana ($0.36).

States with the highest beer taxes on a per-gallon basis are Alaska ($1.07), Alabama ($1.05), Georgia ($1.01), Hawaii ($0.93) and South Carolina ($0.77). States with the lowest tax on beer are Wyoming ($0.02), Wisconsin ($0.06), Missouri ($0.06), Colorado ($0.08), Kentucky ($0.08) and Pennsylvania ($0.08). The states with the highest spirits taxes per gallon are Washington ($26.45), Oregon ($24.63), Virginia ($20.13), Alabama ($18.87) and North Carolina ($13.32).

Property Tax Index

The Property Tax Index is the fifth and final component index that comprises the 2009 State Business Tax Climate Index. The Property Tax Index is comprised of taxes levied on the wealth of individuals and businesses. These include taxes on real and personal property, net worth, and the transfer of assets.

Real and personal property taxes are a contentious subject at the state and local levels as individuals and businesses protest rising tax bills caused by revaluations of residential and business property. In fact, the Tax Foundation's Survey of Tax Attitudes found that local property taxes are perceived as the second most unfair state or local tax.[24] Taxes increase as property values rise unless new, higher assessments are matched by a decrease in the rate.

GENERATION SKIPPING TAX

This will be the first year that a variable has been rendered obsolete for the State Business Tax Climate Index. Nebraska has for the last few years been the lone hold-out maintaining the generational skipping tax. The generational skipping tax is levied on bequests of assets to grandchildren. This variable is just one of many distortive taxes associated with bequests included the SBTCI. The other taxes are the gift tax, the inheritance tax and the estate tax.

Property taxes are especially important to businesses because the tax rate on commercial property is generally higher than on residential property. Additionally, localities and states often levy taxes on the personal property or equipment owned by a business. Since property taxes can be a large burden to business, they can have a significant effect on location decisions.

Mark, McGuire and Papke (2000) find taxes that vary from one location to another within a region could be important determinants of intraregional location decisions. They find that higher rates of two business taxes—the sales tax and the personal property tax—are associated with lower employment growth. They estimate that a tax hike on personal property of one percentage point reduces annual employment growth by 2.44 percentage points (Mark et al. 2000).

Personal property taxes are levied on assets of individuals and business. They can be on assets ranging from cars to machinery and equipment to office furniture and fixtures, but are separate from real property taxes which are taxes on land and buildings. These findings provide strong evidence that personal property taxes significantly affect business decisions. Furthermore, these findings suggest that states competing for business would be well served to keep statewide property taxes low so as to be more attractive to business investment.

24 Matt Moon, "How do Americans Feel about Taxes Today? Tax Foundation's 2009 Survey of U.S. Attitudes on Taxes, Government Spending and Wealth Distribution," *Tax Foundation Special Report,* No. 166, April 2009

Localities competing for business can put themselves at greater competitive advantage by keeping personal property taxes low as well.

Bartik (1985), finding that property taxes are a significant factor in business location decisions, estimates that a 10 percent increase in business property taxes decreases the number of new plants opening in a state by between 1 and 2 percent. Bartik (1989) backs up his earlier findings by concluding that higher property taxes negatively affect small business starts. He elaborates that the particularly strong negative effect of property taxes occurs because they are paid regardless of profits, and many small businesses are not profitable in their first few years, so high property taxes would be more influential than profit-based taxes on the start-up decision.

Businesses remitted $554 billion in state and local taxes in fiscal year 2006, of which 37 percent or $204.8 billion was for property taxes. The property taxes included tax on real, personal, and utility property owned by business (Cline et al. 2007). Obviously property taxes are a significant cost to business. Coupled with the academic findings that property taxes are the most influential tax in terms of impacting location decisions by businesses, the evidence supports the conclusion that property taxes are a significant factor in a state's business tax climate.

The Property Tax Index factors in more than just taxes on real estate and personal property. Taxes on capital stock, intangible property, inventory, real estate transfers, estates, inheritance, and gifts are also included. The generation-skipping tax has been dropped from the index because Nebraska, the last state to have one on the books repealed its tax before the beginning of the 2010 fiscal year.

WISCONSIN

Wisconsin dropped three spots this year to finish with a rank of 42nd best. The blame for Wisconsin's drop falls on the creation of a new income tax bracket: 7.75 percent on taxable income over $225,000.

The top five states this year in terms of a favorable Property Tax Index were New Mexico, Utah, Idaho, Arizona and North Dakota. These are the same states reported in last year's Index. They continue to have low property tax rates when measured on a per capita basis or as a percentage of income. Additionally, these states avoid taxes like estate, inheritance, and gift which distort economic decision-making.

Four of the five states at the bottom of the index are the same as last year. New Jersey, Ohio, Connecticut and Rhode Island continue to score near the bottom of the Property Tax Index. These states have consistently high rates of property tax and taxes on estates, inheritance and other forms of property. Tennessee was included among the bottom five states for the first time this year.

The Property Tax Index is comprised of two equally weighted sub-indexes devoted to measuring the economic damage of the rates and the tax bases. The rate sub-index consists of property tax collections, capital stock tax rates, and maximum payments. The base portion consists of dummy variables detailing whether each state levies wealth taxes, such as inheritance or estate, gift, inventory, intangible property and other similar taxes. The entire Property Tax Index is weighted at 15.48 percent of each state's overall State Business Tax Climate score. See Table 21 and 22 for details of each state's property taxes.

Sub-Index #1: The Property Tax Rate

The property tax rate sub-index consists of property tax and capital stock tax sub-indices. Property taxes are measured by dollars collected per capita and as a percentage of personal income. Both measures are weighted equally and receive 80 percent of the total weight of the rate sub-index. The reason for this weighting is to reflect the importance to businesses and individuals of the increasing size and visibility of property taxes. New Mexico, Kentucky, Delaware, Alabama and Utah scored the best for having consistently low property tax rates. Additionally, their capital stock rate is either zero or with a low rate and maximum payment. The opposite of this is true with states that scored poorly on the rate sub-index. New Jersey, Wyoming, New Hampshire, Connecticut and Rhode Island were the worst performers this year.

Property Tax Collections and Rates

The property tax rate sub-index is weighted at 50 percent for each section: property tax collections per capita and property tax collections as a percentage of personal income. Both are included to gain a better understanding of how much each state collects in proportion to its population and its income. The per capita figure lets taxpayers know how much in actual dollar terms they pay in property taxes compared to residents of other states. Tax collections measured as a percentage of personal income gives taxpayers a sense of how much of their income is devoted to property taxes.

While the tax measures are not ideal—having effective tax rates of personal and real property for both businesses and individuals would be ideal—they are the best measures reasonably available. Due to the research challenge posed by the

thousands of jurisdictions in the country that levy property taxes, the few studies that address this subject have used representative towns or cities instead of the entire state. The best source for data on property taxes is the U.S. Bureau of Census since it can collect and compile the data and reconcile any definitional problems.

States that maintain low effective rates and low collections per capita are more likely to promote economic growth than states with high rates and collections. Alabama, Delaware, New Mexico, Arkansas and Oklahoma were states that scored best in terms of property collections and rates. These five states all had consistently low rates for both the per capita amount and effective percent of income. The opposite was true of the poorly performing states where collections per capita and effective rates were high.

Property Tax Collections Per Capita

Property tax collections per capita are calculated by dividing the amount of property tax collected in each state (obtained from the Census Bureau) by the state population. The states that paid the highest property taxes per capita were New Jersey ($2,635), Connecticut ($2,386), New Hampshire ($2,304), Wyoming ($2,118) and Rhode Island ($2,096). The states that paid the lowest property taxes per capita were Alabama ($471), Arkansas ($519), New Mexico ($529), Oklahoma ($554) and Kentucky ($611).

Effective Property Tax Rate

Property tax collections as a percentage of personal income are derived by dividing the Census Bureau's figure for total property tax collections by personal income in each state. This provides the effective property tax rate. States with the highest effective rates and therefore the worst scores are New Hampshire (5.96 percent), New Jersey (5.82 percent), Vermont (5.80 percent), Maine (5.77 percent) and Rhode Island (5.36 percent). Delaware (1.23 percent), Alabama (1.59 percent), New Mexico (1.69 percent), Oklahoma (1.86 percent), and Arkansas (1.86 percent) were the states with the lowest effective property tax rates and the best scores.

Capital Stock Taxes

Capital stock taxes are often referred to as franchise taxes. These are taxes levied on the wealth of a corporation, usually defined as net worth. They are often levied in addition to corporate income taxes, adding a duplicate layer of taxation and compliance for many corporations. A corporation's financial troubles can be exacerbated when it has to use available cash flow to pay its capital stock tax. In assessing capital stock taxes, the sub-index accounts for three variables: the capital stock tax rate, maximum payment and a capital stock tax versus corporate income tax dummy variable. The capital stock tax sub-index is 20 percent of the total rate sub-index.

Capital Stock Tax Rate

The variable measures the rate of taxation levied by the 22 states that have a capital stock tax. The damaging effects of a capital stock tax are beginning to be noted by a number of state legislatures. West Virginia's current rate of 0.55 percent will be phased down to 0.21 percent in 2013. Pennsylvania and Kansas are both in the process of phasing out their capital stock tax altogether. States with the highest capital stock tax rates for 2010 are West Virginia (0.55 percent), Connecticut (0.31 percent), Arkansas (0.3), Louisiana (0.3 percent), and Massachusetts (0.26 percent).

Maximum Capital Stock Tax Payment

Nine states mitigate the negative economic impact of the capital stock tax by placing a cap on the annual capital stock tax payment: Alabama, Connecticut, Delaware, Georgia, Illinois, Kansas, North Carolina, Oklahoma and Oregon.

Capital Stock Tax as an Alternative to the Corporate Income Tax

Aside from establishing a maximum payment in law, four states have mitigated the negative economic impact of their capital stock taxes by allowing businesses to pay only the higher of their two principal business taxes, either the capital stock tax or corporate income tax. Connecticut, New York, Ohio and Rhode Island receive a higher score for this variable than states that states that demand payment of both each year. States that do not have a capital stock tax get the best scores.

Sub-Index #2: The Property Tax Base

The property tax base index makes up the remaining 50 percent of the Property Tax Index. The sub-index is composed of dummy variables listing the different types of property taxes levied by each state. Nine states receive a perfect score because they do not implement any of the six different kinds of property tax: Alaska, Arizona, Colorado, Idaho, Missouri, Montana, New Mexico, North Dakota, Utah States with a high rate of or a complex, multiple-rate system score poorly. and Wyoming. The states that score the worst because they impose several of these taxes are Tennessee, North Carolina, Ohio, Iowa, Maryland,

Kentucky, Nebraska, New Jersey, Oklahoma and Pennsylvania.

Personal Property Taxes

Intangible Property Tax

This dummy variable punishes those states that impose taxes on intangible personal property. Intangible personal property includes things such as stocks, bonds, and even trademarks. This tax can be harmful to businesses that hold large amounts of their own or other companies' stock and that have valuable trademarks. Ten states levy this punitive tax: Alabama, Georgia, Iowa, Louisiana, Mississippi, North Carolina, Ohio, Pennsylvania, Tennessee and Texas.

Inventory Tax

Levied on the value of a company's inventory, the inventory tax is especially harmful to large retail stores and other businesses that store large amounts of merchandise. Inventory taxes distort market signals because they force companies to make production decisions that are not entirely based on economic principles, but rather on how to pay the least amount of tax on goods produced. Inventory taxes also create a strong incentive for companies to locate their inventory in states where they can avoid the tax. This tax can be unproductive for the company when inventories are located in less profitable locations and for state governments that lose economic activity by imposing the tax. Fifteen states levy inventory taxes.

Asset Transfer Taxes

Four taxes levied on the transfer of assets are part of the Property Tax Index base. These taxes all increase the cost and complexity of transferring wealth and hurt a state's business climate. These harmful effects can be particularly acute in the case of small, family-owned businesses. The four taxes are real estate transfer taxes, estate taxes, inheritance taxes and gift taxes. Thirty-five states and the District of Columbia levy taxes on the transfer of real estate that can add as much as 2.2 percent to the price of the property.

Estate taxes are among the most complex individual taxes, and state-level estate taxes have an added layer of complexity due to their interconnectedness with the federal estate tax and the changes in federal law brought about by the Economic Growth and Tax Relief Reconciliation Act (EGTRRA) of 2001. Before 2001, most states piggy-backed on the federal system. Since the federal system allowed a credit for state estate taxes paid, the federal government was essentially paying the states' estate tax collections, and taxpayers did not object because their tax liabilities were unchanged.

EGTRRA was designed to gradually phase out the federal estate tax, with total repeal in 2010. But even before 2010, EGTRRA repealed the credit for state estate taxes paid. Facing the loss of a revenue source, states began to "decouple," that is, to re-write their own estate taxes so that they didn't depend on the existence of the federal estate tax. The 33 states that allowed their own estate taxes to expire with the federal credit in 2005 get a positive score. Seventeen states have decoupled from the federal system to maintain the revenue stream of estate taxes by either reverting to pre-EGTRRA rules or creating their own stand-alone system. These states are punished in the index for increasing complexity.

The estate tax can disproportionately hurt small-to-medium sized businesses whose owners have not availed themselves of the costly estate planning and insurance policies whose necessity is well understood by families whose wealth is longstanding. As a result, smaller businesses often make surprisingly large estate tax payments.

Inheritance taxes are similar to estate taxes, but they are levied on the heirs of an estate, instead of on the estate itself. Therefore, a person could inherit a family-owned company from his or her parents and be forced to downsize or sell part or all of it in order to pay the heir's inheritance tax. Eight states have inheritance taxes and are scored lower in the index accordingly.

The final asset transfer tax included in the property tax base sub-index is the gift tax. From the tax collector's perspective, a gift tax is designed to prevent individuals from giving away their estates before they die to avoid the estate taxes, but transfers with other motivations also trigger a tax liability. A state's business tax climate is affected most often when the gift tax is levied on individuals who own sole proprietorships, or who are partners in other non-corporate businesses, such as S-corps and LLCs. The three states that currently levy a gift tax are Connecticut, North Carolina and Tennessee.

Unemployment Insurance Tax Index

The Unemployment Insurance Tax Index is the fifth and final component index. Unemployment insurance taxes are paid by the employer and finance benefits for recently unemployed workers.

Every state has some form of unemployment insurance tax, and all are complex systems that impose different tax rates depending on each industry and even firms within an industry. The rate rises when the state's unemployment insurance trust fund is low or if a particular firm or industry has a history of rapid turnover.

One of the worst aspects of the unemployment insurance tax system is its application to financially troubled businesses. When a firm is laying workers off to survive, that is when it is forced into higher tax rate schedules. This phenomenon—a business being forced to pay higher unemployment insurance taxes just when it is losing money and at risk of bankruptcy—is known as the shut-down effect. These taxes leave companies unable to sufficiently lower their costs in times of economic recession.

Like the previous four component indexes, the Unemployment Insurance Tax Index consists of two sub-indexes, one that measures each state's rate structure and one that focuses on the tax base. Each is weighted to represent half of the total index score.

For a state to score high on the index, its unemployment tax should be as simple as possible, within the constraints of federal law. This means having minimum and maximum rates and a wage base at the federal level. The experience formulas and charging methods of an efficient unemployment insurance tax are not complicated and do not have benefit add-ons or surtaxes. The states that score the best are Oklahoma, Arizona, Florida, Mississippi and North Carolina.

On the other side of the coin, Rhode Island, Massachusetts, New York, Illinois and Michigan all scored poorly on the Unemployment Insurance Tax Index. These states tend to have rate structures with high minimum and maximum rates and wage bases above the federal level. Moreover, they have more complicated experience formulas and charging methods. The Unemployment Insurance is weighted at 11.36 percent of the total score.

Sub-Index #1: Unemployment Insurance Tax Rate

Unemployment insurance tax rates in each state are based on a schedule from minimum to maximum rates. The schedule for any particular business is dependent upon the business's experience rating. The rate is then applied to a taxable wage base (a predetermined fraction of an employee's wage) to determine unemployment insurance tax liability.

Overall, the states with the best score on this sub-index are Arizona, Florida, Georgia, Colorado and Texas. These states all have low rates and wages schedules. To contrast this, Massachusetts, Rhode Island, Minnesota, Pennsylvania and Kentucky have higher rates and score the worst.

Tax Rates in the Most Recent Year

Minimum Tax Rate

States with the best scores for the minimum tax rate variable are Colorado, Hawaii, Kansas, Missouri, Montana, North Carolina, South Dakota and Washington with a minimum rate of zero. The highest rates and therefore worst scores are found in Pennsylvania (1.84 percent), Rhode Island (1.69 percent), California (1.50 percent), West Virginia (1.50 percent) and South Carolina (1.24).

Maximum Tax Rate

Fifteen states receive the highest score for the maximum tax rate variable. They have a relatively low tax rate of 5.4 percent.[25] The state are Alaska, Arizona, Colorado, Florida, Georgia, Hawaii, Idaho, Maine, Mississippi, Nebraska, Nevada, New Jersey, New Mexico, Oregon and Washington. States with the highest rates and thus the worst scores on this variable are Massachusetts (10.96 percent), Minnesota (10.70 percent), Michigan (10.30 percent), Tennessee (10.00 percent) and Pennsylvania (9.98 percent).

Taxable Wage Base

Eight states receive the best score for the taxable wage base variable. They had a taxable wage base of $7,000 which corresponds with the federal taxable wage base. The states with the highest taxable bases and thus the worst scores on this variable are Washington ($35,700), Idaho ($33,200), Alaska ($33,200), Oregon ($31,300) and New Jersey ($28,900).

Potential Rate

Due to business and seasonal cycles, all the businesses in each state will probably be forced to

25 The federal government levies its own UI tax called the Federal Unemployment Tax Act (FUTA) with a rate of 6.2 percent on wages up to $7,000. However, the federal government provides a tax credit worth up to 5.4 percent on the wage base. As a result, the lowest state maximum rate is 5.4 in order to maximize the use of the federal credit. Therefore, the effective federal rate is a much lower 0.8 percent and is used predominantly to offset the administrative costs associated with oversight of the unemployment trust fund.

change unemployment insurance tax rate schedules at some point each year. When unemployment insurance trust funds are flush, businesses will trend toward the most favorable rate schedules; however, when trust funds are low, businesses will trend toward the least favorable rate schedules. Not only are the rates themselves important from a neutrality perspective, but states with a wide range between the minimum and maximum rates are less neutral than states with a narrow range. Consequently we prepare minimum and maximum index variables for both the most favorable tax rate schedule and the least favorable tax rate schedule.

Most Favorable Tax Rate Schedule

Minimum Tax Rate Schedule

Twenty states have a minimum tax rate of zero when unemployment is low and the unemployment insurance trust fund is flush. These states score the best for this variable. The states with the highest minimum tax rates and thus the worst scores are Massachusetts (0.8 percent), Rhode Island (0.6 percent), South Carolina (0.54 percent), Oregon (0.5 percent) and Connecticut (0.5 percent).

Maximum Tax Rate Schedule

Twenty-three states receive the best score for the most favorable maximum tax rate variable. They have a comparatively low maximum tax rate of 5.4 percent. The states with the highest minimum tax rates and thus the worst score are Michigan (10.3 percent), Tennessee (10 percent), Wyoming (10 percent), Kentucky (10 percent), Minnesota (10 percent) and Utah (10 percent).

Least Favorable Tax Rate Schedule

Minimum Tax Rate Schedule

Four states receive the best score in this variable with a minimum tax rate of zero percent: Iowa, Missouri, Nebraska and North Carolina. The states with the highest minimum tax rates and the worst minimum tax scores are New Mexico (2.7 percent), Hawaii (2.4 percent), Oregon (2.2 percent), Maryland (2.2 percent), Connecticut (1.9 percent) and Rhode Island (1.9 percent).

Maximum Tax Rate Schedule

Eleven states receive the best score in this variable with a comparatively low maximum tax rate of 5.4 percent. The states with the highest maximum tax rates and the worst tax scores are Massachusetts (15.4 percent), Maryland (13.5 percent), Arkansas (10.8 percent) and Michigan (10.3 percent).

Sub-Index #2: Unemployment Insurance Tax Base

The Unemployment Insurance Tax sub-index assesses states on how they determine business's unemployment insurance tax. It takes into account which businesses should pay the tax and how much, as well as other unemployment insurance taxes that a business may also be liable.

The states that received the best score on this sub-index are Oklahoma, Connecticut, Arizona, California and Missouri. In general, these states have relatively simple experience formulas. These states exclude more factors from their charging method and levy fewer surtaxes.

States that receive the worst scores are Virginia, New Hampshire, New York, Rhode Island, Idaho and Illinois. They have more complicated experience formulas, exclude fewer factors from the charging method, and have complicated their systems with add-ons and surtaxes. The three equally weighted factors considered in this sub-index are experience rating formulas, charging methods, and a host of smaller factors aggregated into one variable.

Experience Rating Formula

A business's experience rating formula determines the rate the firm must pay and affects whether it will lean towards the minimum rate or the maximum rate of the given schedule.

There are four basic experience formulas: contribution, benefit, payroll and state experience. The first three experience formulas (contribution, benefit and payroll) are based solely on the business's experience and are therefore non-neutral by design. However, the final variable (state experience) is a positive mitigating factor because all businesses are treated equally. In other words, the state experience is not tied to the experience of any one business and is, therefore, a more neutral factor. This sub-index penalizes states that depend on the contribution, benefit and payroll experience variables while rewarding states with the state experience variable.

Charging Methods and Benefits Excluded from Charging

A business's experience rating will vary depending on which charging method the state government uses. When a former employee applies for unemployment benefits, the benefits paid to the employee must be charged to a previous employer. There are three basic charging methods:

1. Charging Most Recent or Principal Employer: Thirteen states charge all the benefits to one employer, usually the most recent.

2. Charging Base-Period Employers in Inverse Chronological Order: Six states charge all base period employers in inverse chronological

Table 7
Unemployment Insurance Tax Index, 2006 – 2010

	FY 2010 Unemployment Insurance Tax Index		FY 2009 Unemployment Insurance Tax Index		Change from 2009 to 2010		FY 2008 Unemployment Insurance Tax Index		FY 2007 Unemployment Insurance Tax Index		FY 2006 Unemployment Insurance Tax Index	
State	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank
US	5.00	–	5.00	–	5.00	–	5.00	–	5.00	–	5.00	–
Alabama	5.51	16	5.57	14	–0.06	–2	5.60	12	6.06	8	6.23	4
Alaska	4.79	29	3.78	47	1.01	18	3.30	48	3.83	45	3.91	43
Arizona	6.41	2	6.41	2	0.00	0	6.42	2	5.96	10	5.91	12
Arkansas	5.41	17	5.08	23	0.33	6	5.09	25	4.49	35	4.05	41
California	5.55	14	5.47	16	0.08	2	5.49	15	5.50	18	5.50	20
Colorado	5.32	20	5.32	19	0.00	–1	5.22	19	5.20	23	5.27	21
Connecticut	4.66	34	5.20	21	–0.54	–13	5.27	18	5.65	16	5.01	26
Delaware	5.63	13	5.88	7	–0.25	–6	5.99	7	5.99	9	5.95	11
Florida	6.20	3	6.20	3	0.00	0	6.22	3	6.49	3	6.62	1
Georgia	5.21	22	5.20	20	0.00	–2	5.21	21	4.69	32	4.64	32
Hawaii	5.66	12	5.66	11	0.00	–1	5.19	22	5.18	24	5.24	22
Idaho	3.98	48	4.01	45	–0.04	–3	4.03	44	3.49	47	3.68	46
Illinois	4.14	46	4.33	43	–0.19	–3	4.29	42	4.47	36	4.34	37
Indiana	5.67	11	5.62	13	0.05	2	5.64	10	5.55	17	6.05	7
Iowa	4.74	33	4.66	35	0.08	2	4.70	37	5.01	27	4.96	28
Kansas	5.91	6	5.85	8	0.06	2	5.74	9	5.78	12	5.72	15
Kentucky	4.63	36	3.52	48	1.11	12	3.59	47	3.35	48	3.35	48
Louisiana	5.79	8	5.76	10	0.03	2	5.79	8	5.95	11	6.01	9
Maine	4.44	40	4.43	40	0.01	0	4.46	40	4.34	40	3.98	42
Maryland	4.56	37	4.79	31	–0.23	–6	4.83	30	4.76	30	5.63	17
Massachusetts	3.02	49	3.04	49	–0.01	0	3.17	49	2.75	49	2.76	49
Michigan	4.15	45	4.00	46	0.16	1	4.01	45	4.22	42	4.18	40
Minnesota	4.56	38	4.52	38	0.04	0	4.58	39	4.35	39	4.55	35
Mississippi	5.99	4	6.02	5	–0.03	1	6.09	5	6.63	2	6.58	2
Missouri	5.87	7	6.16	4	–0.29	–3	6.13	4	6.09	7	6.02	8
Montana	5.29	21	5.37	18	–0.08	–3	5.22	20	5.22	21	5.16	24
Nebraska	5.54	15	5.64	12	–0.10	–3	5.14	17	5.09	26	5.73	14
Nevada	4.38	42	4.37	42	0.01	0	4.44	41	4.29	41	4.26	38
New Hampshire	4.47	39	4.51	39	–0.04	0	4.65	38	3.95	44	3.91	44
New Jersey	4.95	25	5.07	24	–0.12	–1	5.15	23	5.13	25	4.99	27
New Mexico	5.36	19	5.46	17	–0.10	–2	5.60	13	5.66	15	5.60	18
New York	3.98	47	4.03	44	–0.05	–3	3.85	46	3.62	46	3.62	47
North Carolina	5.92	5	6.00	6	–0.08	1	6.04	6	6.19	4	6.13	5
North Dakota	4.80	28	4.66	34	0.14	6	4.87	29	4.37	38	4.46	36
Ohio	5.69	10	5.52	15	0.17	5	5.64	11	5.34	19	5.88	13
Oklahoma	6.52	1	6.67	1	–0.15	0	6.59	1	6.74	1	6.43	3
Oregon	4.79	30	4.82	30	–0.03	0	4.77	32	4.89	29	4.77	30
Pennsylvania	4.41	41	5.02	26	–0.61	–15	5.13	24	5.76	13	5.71	16
Rhode Island	2.80	50	2.58	50	0.22	0	2.62	50	2.18	50	2.33	50
South Carolina	4.18	43	4.40	41	–0.22	–2	4.14	43	3.95	43	3.87	45
South Dakota	4.66	35	4.59	37	0.07	2	4.77	33	4.75	31	4.70	31
Tennessee	4.77	32	4.77	32	0.00	0	4.83	31	4.66	33	4.60	33
Texas	5.77	9	5.78	9	–0.01	0	5.54	14	6.09	6	6.06	6
Utah	4.95	24	4.94	27	0.01	3	4.93	27	5.25	20	5.21	23
Vermont	5.40	18	5.18	22	0.22	4	5.48	16	6.09	5	5.99	10
Virginia	4.17	44	4.84	29	–0.67	–15	4.91	28	5.21	22	5.16	25
Washington	4.90	26	4.63	36	0.27	10	4.74	36	4.45	37	4.24	39
West Virginia	4.79	31	4.75	33	0.04	2	4.76	35	4.66	34	4.57	34
Wisconsin	5.02	23	5.06	25	–0.03	2	5.07	26	5.00	28	4.95	29
Wyoming	4.86	27	4.86	28	0.00	1	4.77	34	5.67	14	5.53	19
District of Columbia	5.11	–	5.02	–	0.09	–	5.04	–	5.00	–	4.96	–

Note: The higher the score, the more favorable a state's tax system is for business. All scores are for fiscal years.
Source: Tax Foundation

order. This means that all employers within a base period of time (usually the last year, sometimes longer) will have the benefits charged against them with the most recent employer being charge the most.

3. Charging in Proportion to Base-Period Wages: Thirty-one states charge in proportion to base period wages. This means that all employers within a base-period of time (usually the last year, sometimes longer) will have the benefits charge against them in proportion to the wages they paid.

None of these charging methods could be called neutral, but at the margin, charging the most recent or principal employer is the least neutral. When a business is faced with the necessity to lay off employees, it knows it will bear the full charge for unemployment benefits. The most neutral of the three methods is the "charging in proportion to base-period wages." When this method is used there is a higher probability of sharing the benefits charges with previous employers.

As a result, the 31 states that charge in proportion to base-period wages receive the best score. The 13 states that charge the most recent or principal employer receive the worst score. The six states that charge the base-period employers in inverse chronological order receive a median score.

Many states also recognize that certain benefit costs should not be charged to employers, especially if the separation is beyond the employer's control. Therefore, this sub-index also accounts for six types of exclusions from benefit charges.

1. Benefit award reversed
2. Reimbursements on combined wage claims
3. Voluntary leaving
4. Discharge for misconduct
5. Refusal of suitable work
6. Continues to work for employer on part-time basis

States are rewarded for each of these exclusions because they nudge the unemployment insurance system toward neutrality. For instance, if benefit charges were levied for employees who voluntarily quit, then industries with high turnover rates, such as retail, would be hit disproportionately harder. States that receive the best score in this category are Ohio, Utah, Vermont, Oregon, Louisiana, Delaware, Missouri and Arizona. Ohio receives a perfect score by charging in proportion to base-period wages and including all six benefit exclusions. On the other hand, the states that receive the worst scores are Alaska, New Hampshire, Kentucky Nevada, New York, Rhode Island and Virginia. All but Alaska charge the most recent or principal employer and forbid most benefit exclusions.[26]

Other Significant Issues

Five of the eight variables in this catch-all category of the sub-index deal with taxes levied on top of the unemployment insurance tax. Even if these taxes are not invoked, states are still penalized for having them on the books.

The states that received the best scores in this category are Kansas, Michigan, Arizona, Georgia, Missouri, Ohio and Vermont. Louisiana, New Jersey and Rhode Island scored the worst.

Solvency Tax

These taxes are levied on employers when a state's unemployment fund falls below some defined level. Seventeen states have solvency taxes though they are given various names in statutory law.

Taxes for Socialized Cost or Negative Balance Employer

These taxes are levied on employers when a state desires to recover costs of providing benefits that are above and beyond the tax collections based on the normal experience process. Ten states have these taxes under a variety of different names.

Loan and Interest Repayment Surtaxes

Taxes levied on employers when a loan is taken from the federal government or when bonds are sold to pay for benefit costs are of two general types. The first is a tax to pay off the federal loan or bond issue. The second is a tax to pay the interest on the federal loan or bond issue. States are not allowed to pay interest costs directly from the state's unemployment trust fund. Twenty-one states have these taxes.

Reserve Taxes

Reserve taxes are levied on employers to be deposited in a reserve fund separate from the unemployment trust fund. Since the fund is separate, the interest earned on it is often used to create funds for other purposes such as job training and/or paying the costs of the reserve tax collection. Only five states have a reserve tax.

26 Alaska is the only state not to use benefit payments in its formula but instead the variation in an employer's payroll form quarter to quarter. This is an extreme violation of tax neutrality since any decision by the employer or employee that would affect payroll may trigger higher UI tax rates. As a result, Alaska scores the worst of all states in this sub-index.

Surtaxes for UI Administration or Non-UI Purposes
Thirty states levy surtaxes on employers. These funds usually cover administration costs but sometimes they are used for job training or special improvements in technology. They are often deposited in a fund outside of the state's unemployment fund.

Temporary Disability Insurance
A handful of states including California, New Jersey, Rhode Island, Hawaii and New York, have established a temporary disability insurance program that augments the unemployment insurance program. It extends benefits to those unable to work because of sickness or injury. No separate tax supports these programs; the money comes right out of the state's unemployment fund. Because the balance of the fund triggers various taxes, the temporary disability insurance is included as a negative factor in the calculation of this sub-index.

Voluntary Contributions
Twenty-seven states allow businesses to make voluntary contributions to the unemployment trust fund. In most cases, these contributions are rewarded with a lower rate schedule, often saving the business more money in taxes than was paid through the contribution. The Index rewards states that allow voluntary contributions because firms are able to pay when they can best afford to instead of when they are financially struggling. This provision helps to mitigate the non-neutralities of the unemployment insurance tax.

Time-Period to Qualify for Experience Rating
Newly formed businesses, naturally, do not qualify for an experience rating because they simply have not been around long enough. Federal rules stipulate that states can levy a "new employer" rate for one to three years, but no less than one year. From a neutrality perspective, however, this new employer rate is non-neutral in almost all cases since the rate is higher than the lowest rate schedule. The longer this rate is in effect, the worse the non-neutrality. As such, the Index rewards states with the minimum one year required to earn an experience rating and penalizes states that require the full three years.

Methodology

The Tax Foundation's 2010 State Business Tax Climate Index is a hierarchical structure built from five component indexes:

- The Corporate Tax Index
- The Individual Income Tax Index
- The Sales Tax Index
- The Unemployment Tax Index
- The Property Tax Index

The choice of these component indexes is based in the economic literature. The component indexes are designed to score between 0 (worst) and 10 (best). Each of these component indexes is further broken down into two equally weighted sub-indexes. The sub-indexes themselves can include several categories and variables under them. Overall, there are 10 sub-indexes and 112 variables. The ranking of the state on each of the five major component indexes is presented in Table 2.

The index is weighted by the variability of the component indexes, instead of weighting them equally and merely summing them. The standard deviation of each component index is calculated and a weight for each component index is created from that measure. The result is a heavier weighting of those component indexes with greater variability.

This weighting procedure helps to improve the overall measure of the State Business Climate Index. A component where the standard deviation is relatively low means that the 50 states are clustered together. The taxes that are closely clustered together are areas of tax law where businesses are more likely to de-emphasize tax factors in their business decisions.

Oregon is an example of the importance of this type of variability-based weighting. Oregon is regionally known for not having a general sales tax. All of the surrounding states have a rate of at least 6 percent. This can attract business and shoppers from across the Pacific Coast region. It is this wide disparity, then, that makes an economic impact.

In contrast to the variability of the sales tax is the uniformity of the unemployment insurance tax. The 50 scores on the UI index are centered tightly around the mean, offering less competitive advantage from state to state. A ranking of these taxes has less importance, then, because a small change in one state's law could change its component index ranking dramatically, but at the same time tell businesses very little about the overall differential between states.

The weights change from year to year, therefore, as the disparity in state rates widen or narrow with new legislation. In 2010, the weighting is as follows:

1. 19.74% – Corporate Income Tax Index
2. 30.09% – Personal Income Tax Index
3. 24.14% – Sales Tax Index
4. 11.36% – Unemployment Insurance Tax Index
5. 14.67% – Property Tax Index

The sub-indexes within each component are both weighted equally, giving equal importance to rate and base issues.

Each of the sub-indexes is composed of one or more variables. There are two types of variables: scalar and dummy variables. A scalar variable has numerical values. If an index is composed of only scalar variables, then they are weighted equally. A dummy variable is one that only has values of 0 or 1. These are designed to facilitate binary, yes-and-no variables. Combining scalar and dummy variables presents problems for developing indexes. The reason is the polarizing nature of dummy variables. To mitigate the effects of this, the Index weights scalar variables at 80 percent and dummy variables at 20 percent.

Relative versus Absolute Indexing

The 2010 State Business Tax Climate Index is designed as a relative index as opposed to an absolute index. This means that each variable is measured relative to the law in other states, not measured against some ideal. The relative scoring scale is from 0 to 10 with zero being the worst among the 50 states but not the worst possible tax.

OHIO

Ohio saw a slight improvement this year, rising from 48 to 47, as its five-year transition from a corporate income tax to a gross receipts tax of 0.26 percent. A number of states added millionaire's brackets, increased the sales tax rate, or enacted any number of miscellaneous tax increases. Ohio's improvement this year can hopefully serve as a catalyst for future improvement in their code.

An example of this can be found with the top rate for the individual income tax. These rates vary from very low in New Hampshire (0.85 percent) to very high in Oregon and Hawaii (11 percent). New Hampshire with the lowest rate receives a 10. Oregon and Hawaii with the highest rate receive a zero. Georgia with a rate of 6 percent comes in almost in the middle with a score of 5.10. Illinois with a flat 3 percent receives a score of 7.96 and Idaho with a top rate of 7.8 percent receives a score to 3.39.

Many states' tax rates are so close to each other that an absolute index would not provide enough information about the differences between the states' tax systems, especially to pragmatic business owners who want to know what states have the best tax system in each region.

Comparing States without a Tax

The benefits of a relative index come with a cost; it's mathematically impossible to compare states with a given tax to states that do not have the tax. Not having a specific tax is equivalent to having a zero rate with a perfectly neutral base. Both of these offer a favorable tax climate for economic growth. For these reasons states that do not have one of the major taxes (individual income, corporate income and sales tax) have a competitive advantage. To approximate this advantage, states without a given tax receive a value of 10. The Index measures all the other states against each other.

Normalizing Final Scores

Another limitation of using a relative scale within the component indexes is the comparability of scores across the five component indexes. This alters the value of not having a given tax across major indexes. Unadjusted average scores would not be comparable and thus of little use. For example, the unadjusted average score of the Property Tax Index is 6.96 while the average score of the Sales Tax Index is 5.36.

In order to resolve this problem, scores on the five major component indexes are "normalized," which brings the average score for all of them to 5.00—excluding states that do not have the given tax. This is accomplished by multiplying every state's score by a constant value.

Once the scores are normalized, it is possible to compare states across indexes. For example, because of normalization it is possible to say that Oregon's score of 3.43 on the Individual Income Tax is worse than its score of 9.07 on the Sales Tax.

Time Frame Measured by the SBTCI

Annually, the State Business Tax Climate Index takes a snapshot of each state's business tax climate at the start of the standard fiscal year, July 1. Thus, this 2010 edition represents our estimation of each state's business tax climate on July 1, 2009.

The District of Columbia

The District of Columbia is not included in the relative scores calculation. It is included for exhibition purposes only.

Changes in the Index

One significant change to this year's Index was dropping the generation-skipping tax variable

from the Property Tax Index. Nebraska had been the sole holdout for this distortionary tax but repealed it last year and thus eliminated all variance in the variable. A major improvement this year is a superior calculation of local option sales tax rates. Previously, this had been a weighted average of county level data. This county level data misses much variability of local municipalities. The Tax Foundation was able to acquire local sales tax data by 5 digit zip codes. This new data set allows a much more accurate measure of local sales tax.

Conclusion

The Tax Foundation's State Business Tax Climate Index is designed to assist legislators and business leaders in determining the relative merits of a state's tax environment. Clearly, tax policy is not the sole determinant of business climate. Many features of a state's population, geography and economy factor into the decision of where a business locates or expands: proximity to consumers and raw materials, labor markets and regulation, just to name a few. However, tax policy has repeatedly been shown to be a significant factor in business decisions.

Every state must raise revenue, and thus every state must tax. No state, however, needs to tax in a way that has significant adverse effects on the business climate. A state needs to continually strive for a tax system that is neutral and pro-growth. A neutral tax system is one in which specific economic activities are not targeted for exemptions or selective taxes. A pro-growth system will avoid excessive taxes and compliance costs on businesses.

States that have scored poorly this year can use the 2010 State Business Tax Climate Index to find targets for improvement. The advantage of this Index is that it can show poorly performing states where they do well. Maryland scored 44th best this year, but its sales tax comes in at an impressive 10th best. On the other hand, legislators there could consider attempting reform of the individual income tax that ranked #49. Poorly performing states are not the only ones that can benefit from the Index. States that score well can improve their competitive advantage. Wyoming was ranked #2 this year but was ranked #36 on the property tax index.

Currently the economic conditions for many states are not good, with high unemployment and falling state GDP. This has led to revenue shortfalls for many states. Now is the time for states to undertake fundamental tax reform and not short-run tax gimmicks. A tax system based on sound principles will be the best way for states to insure long-run, stable growth in the future.

Appendix 1: Pending and Proposed Tax Changes Not Reflected in the 2010 State Business Tax Climate Index

The 2010 State Business Tax Climate Index depicts each state's tax system as it stood on July 1, 2009 – the first day of the 2010 fiscal year. Several states didn't finish their budgeting on time, though, so here we comment on how laws enacted after July 1 could be expected to affect the tax climate.

No definitive claims can be made about how a particular change could affect a future ranking because other states may improve or damage their business tax climates in the meantime; we categorize proposed changes here as ones that are likely to improve or worsen a state's tax climate.

Changes Likely to Improve a State's Tax Climate

Kansas

Kansas continues to phase out its franchise tax, which is categorized with capital stock taxes in the Property Tax Index. The franchise tax rate, set at 0.125 percent for 2007 has continued to fall. The franchise tax currently is 0.03125%. In 2011 the tax will be fully repealed, and Kansas is likely to improve its score on the Property Tax Index as Kansas joins the other 28 states that do without a capital stock-style tax.

Pennsylvania

Like Kansas, Pennsylvania is currently in the process of phasing out the capital stock tax by 2011. Pennsylvania's Property Tax Index score should improve as repeal approaches.

West Virginia

In 2006 and prior, West Virginia had one of the country's highest corporate income tax rates, at 9%. The rate is now 8.5% and will continue to fall to 7.75% in 2012, 7% in 2013, and 6.5% in 2014. Its franchise tax is still the highest in the country at 0.55% (Formerly 0.7%), but it will fall gradually until it reaches 0.21% in 2013. As these rates continue to fall, West Virginia should see continued improvement on its Corporate Income and Property Tax scores.

Changes Likely to Hurt a State's Tax Climate

Connecticut

Connecticut is currently considering the creation of a new top bracket of income greater than $500,000 for single filers and $1,000,000 for married couples. The new millionaire's rate would be 6.5%, almost a third higher than the 5% rate that applied on July 1. This new bracket will hurt Connecticut's score under several subindexes of the Personal Income Tax Index.

District of Columbia

The District of Columbia enacted a number of taxes on August 26, 2009 in order to close a budget gap. These included an increase in the sales tax from 5.75% to 6%. In addition to the general sales tax hike, the city also raised several selective sales taxes, or excise taxes as they are often called. The tax on a pack of cigarettes went up $0.50, and the tax on motor fuel increased from $0.20 to $0.235.

Appendix 2: Components of the State Business Tax Climate Index

Table 8
State Corporate Tax Rates
As of July 1, 2009

State	Corporate Income Tax Rates and Brackets			Gross Receipts Tax Rate (a)
Alabama	6.5%	>	$0	
Alaska	1%	>	$0	
	2%	>	$10,000	
	5%	>	$20,000	
	4%	>	$30,000	
	5%	>	$40,000	
	6%	>	$50,000	
	7%	>	$60,000	
	8%	>	$70,000	
	9%	>	$80,000	
	9.4%	>	$900,000	
Arizona	6.97%	>	$0	
Arkansas	1%	>	$0	
	2%	>	$3,000	
	3%	>	$6,000	
	5%	>	$11,000	
	6%	>	$25,000	
	6.5%	>	$100,000	
California	8.84%	>	$0	
Colorado	4.63%	>	$0	
Connecticut	7.5%	>	$0	
Delaware	8.7%	>	$0	0.576%
Florida	5.5%	>	$0	
Georgia	6%	>	$0	
Hawaii	4.4%	>	$0	
	5.4%	>	$25,000	
	6.4%	>	$100,000	
Idaho	7.6%	>	$0	
Illinois	7.3%	>	$0	
Indiana	8.5%	>	$0	
Iowa	6%	>	$0	
	8%	>	$25,000	
	10%	>	$100,000	
	12%	>	$250,000	
Kansas	4%	>	$0	
	7.05%	>	$50,000	
Kentucky	4%	>	$0	0.095%
	5%	>	$50,000	
	6%	>	$100,000	
Louisiana	4%	>	$0	
	5%	>	$25,000	
	6%	>	$50,000	
	7%	>	$100,000	
	8%	>	$250,000	
Maine	3.5%	>	$0	
	7.93%	>	$25,000	
	8.33%	>	$75,000	
	8.93%	>	$250,000	
Maryland	8.25%	>	$0	
Massachusetts (b)	9.5%	>	$0	
Michigan (c)	4.95%	>	$0	
Minnesota	9.80%	>	$0	0.98%

Mississippi	3%	>	$0	
	4%	>	$5,000	
	5%	>	$10,000	
Missouri	6.25%	>	$0	
Montana	6.75%	>	$0	
Nebraska	5.58%	>	$0	
	7.81%	>	$50,000	
Nevada		None		
New Hampshire (d)	8.5%	>	$50,000	0.75%
New Jersey	6.76%	>	$0	
	7.8%	>	$50,000	
	9.36%	>	$100,000	
New Mexico	4.8%	>	$0	
	6.4%	>	$500,000	
	7.6%	>	$1,000,000	
New York	7.1%	>	$0	
North Carolina	6.9%	>	$0	
North Dakota	2.6%	>	$0	
	4.10%	>	$3,000	
	5.6%	>	$8,000	
	6.4%	>	$20,000	
	6.5%	>	$30,000	
Ohio	2.04%	>	$0	0.208%
	3.4%	>	$50,000	
Oklahoma	6%	>	$0	
Oregon	6.6%	>	$0	
	7.9%	>	$250,000	
Pennsylvania	9.99%	>	$0	
Rhode Island	9%	>	$0	
South Carolina	5%	>	$0	
South Dakota		None		
Tennessee	6.5%	>	$0	
Texas		None		1%
Utah	5%	>	$0	
Vermont	6%	>	$0	
	7%	>	$10,000	
	8.5%	>	$25,000	
Virginia	6%	>	$0	
Washington		None		0.484%
West Virginia	8.7%	>	$0	
Wisconsin	7.9%	>	$0	
Wyoming		None		
District of Columbia	9.98%	>	$0	

Note: Corporations pay many types of taxes, of which the corporate income tax is usually the most important for the business tax climate. However, some states levy other important business taxes such as the franchise tax and capital stock tax. Many of these are “wealth taxes” with a tax baseconsisting of capital assets, stocks, property, etc. The Business Tax Climate Index tallies these in the Property Tax Index rather than in the Corporate Tax Index.

(a) Most state collect tax as a percentage of gross receipts from public utilities and some other sectors, and most states have a business license fee or other fixed dollar amount that all businesses must pay, and sometimes those are called gross receipts taxes. Shown here are only states that tax all business broadly as a percentage of gross receipts.

(b) Includes 14 percent surcharge

(c) Includes 21.99 percent surtax

(d) New Hampshire has a dual corporate income tax with differing tax bases - the business profit tax (BPT) and business enterprise tax (BET). The BPT has a rate of 8.5 percent if gross income is over $50,000 and the BET has a rate of 0.75 percent if gross income is over $150,000 or base (total compensation, interest and dividends paid over $75,000.

Sources: Tax Foundation, Commerce Clearing House, state tax forms

Table 9
Business Tax Base Criteria: Credits and Deductions
As of July 1, 2009

State	Job Credits	Research and Development Credits	Investment Credits	Compensation Expenses Deductible	Cost of Goods Sold Deductible
Alabama	Yes	Yes	Yes	Yes	Yes
Alaska	No	No	No	Yes	Yes
Arizona	No	Yes	Yes	Yes	Yes
Arkansas	Yes	Yes	Yes	Yes	Yes
California	Yes	No	No	Yes	Yes
Colorado	Yes	Yes	No	Yes	Yes
Connecticut	Yes	Yes	Yes	Yes	Yes
Delaware	Yes	Yes	Yes	No	No
Florida	Yes	Yes	Yes	Yes	Yes
Georgia	Yes	Yes	Yes	Yes	Yes
Hawaii	Yes	No	Yes	Yes	Yes
Idaho	Yes	Yes	Yes	Yes	Yes
Illinois	Yes	Yes	Yes	Yes	Yes
Indiana	Yes	Yes	Yes	Yes	Yes
Iowa	Yes	Yes	Yes	Yes	Yes
Kansas	Yes	Yes	Yes	Yes	Yes
Kentucky	Yes	Yes	Yes	No	Yes
Louisiana	Yes	Yes	Yes	Yes	Yes
Maine	Yes	Yes	Yes	Yes	Yes
Maryland	Yes	Yes	Yes	Yes	Yes
Massachusetts	Yes	Yes	Yes	Yes	Yes
Michigan	Yes	No	Yes	No	Yes
Minnesota	Yes	Yes	No	Yes	Yes
Mississippi	Yes	Yes	Yes	Yes	Yes
Missouri	No	Yes	Yes	Yes	Yes
Montana	Yes	Yes	Yes	Yes	Yes
Nebraska	Yes	Yes	Yes	Yes	Yes
Nevada	n.a	n.a	n.a	n.a	n.a
New Hampshire	Yes	Yes	No	No	Yes
New Jersey	Yes	Yes	Yes	Yes	Yes
New Mexico	No	Yes	Yes	Yes	Yes
New York	Yes	Yes	Yes	Yes	Yes
North Carolina	Yes	Yes	Yes	Yes	Yes
North Dakota	Yes	Yes	Yes	Yes	Yes
Ohio	Yes	Yes	Yes	No	No
Oklahoma	No	No	Yes	Yes	Yes
Oregon	Yes	Yes	Yes	Yes	Yes
Pennsylvania	Yes	Yes	No	Yes	Yes
Rhode Island	Yes	Yes	Yes	Yes	Yes
South Carolina	Yes	Yes	No	Yes	Yes
South Dakota	n.a	n.a	n.a	n.a	n.a
Tennessee	Yes	Yes	No	Yes	Yes
Texas	No	Yes	Yes	Partial (a)	Partial (a)
Utah	Yes	Yes	No	Yes	Yes
Vermont	Yes	Yes	Yes	Yes	Yes
Virginia	Yes	No	No	Yes	Yes
Washington	Yes	Yes	Yes	No	No
West Virginia	Yes	Yes	Yes	Yes	Yes
Wisconsin	Yes	No	Yes	Yes	Yes
Wyoming	n.a	n.a.	n.a.	n.a.	n.a.
Dist. of Columbia	Yes	No	No	Yes	Yes

(a) Businesses may deduct either compensation or cost of goods sold but not both
Source: Tax Foundation, CCH

Table 10
Other Business Tax Base Criteria
As of July 1, 2009

State	Carry-back (Years)	Carry-forward (Years)	Carry-back Cap	Carry-forward Cap
Alabama	0	15	$0	Unlimited
Alaska	2	20	Unlimited	Unlimited
Arizona	0	5	$0	Unlimited
Arkansas	0	5	$0	Unlimited
California	0	20	$0	Unlimited
Colorado	0	20	$0	Unlimited
Connecticut	0	20	$0	Unlimited
Delaware	2	20	$30,000	Unlimited
Florida	0	20	$0	Unlimited
Georgia	2	20	Unlimited	Unlimited
Hawaii	2	20	Unlimited	Unlimited
Idaho	2	20	$100,000	Unlimited
Illinois	0	12	$0	Unlimited
Indiana	2	20	Unlimited	Unlimited
Iowa	2	20	Unlimited	Unlimited
Kansas	0	10	$0	Unlimited
Kentucky	0	20	$0	Unlimited
Louisiana	3	15	Unlimited	Unlimited
Maine	0	20	$0	Unlimited
Maryland	2	20	Unlimited	Unlimited
Massachusetts	0	5	$0	Unlimited
Michigan	0	10	$0	Unlimited
Minnesota	0	15	$0	Unlimited
Mississippi	2	20	Unlimited	Unlimited
Missouri	2	20	Unlimited	Unlimited
Montana	3	7	Unlimited	Unlimited
Nebraska	0	5	$0	Unlimited
Nevada	n.a.	n.a.	n.a.	n.a.
New Hampshire	0	10	$0	$1,000,000
New Jersey	0	7	$0	Unlimited
New Mexico	0	5	$0	Unlimited
New York	2	20	$10,000	Unlimited
North Carolina	0	15	$0	Unlimited
North Dakota	0	20	$0	Unlimited
Ohio	0	20	$0	Unlimited
Oklahoma	2	20	Unlimited	Unlimited
Oregon	0	15	$0	Unlimited
Pennsylvania	0	20	$0	$3,000,000
Rhode Island	0	5	$0	Unlimited
South Carolina	0	20	$0	Unlimited
South Dakota	n.a.	n.a.	n.a.	n.a.
Tennessee	0	15	$0	Unlimited
Texas	0	5	$0	Unlimited
Utah	3	15	$1,000,000	Unlimited
Vermont	0	10	$0	Unlimited
Virginia	2	20	Unlimited	Unlimited
Washington	3	20	Unlimited	Unlimited
West Virginia	2	20	$300,000	Unlimited
Wisconsin	0	15	$0	Unlimited
Wyoming	n.a.	n.a.	n.a.	n.a.
Dist. of Columbia	0	20	$0	Unlimited

Source: CCH.

Table 11
Other Business Tax Base Criteria
As of July 1, 2009

State	Federal Income Used as State Tax Base	Allows Federal ACRS or MACRS Depreciation	Allows Federal Depletion	Throwback Rule	Foreign Tax Deductibility	Corporate AMT	Brackets Indexed for Inflation
Alabama	Yes	Yes	No	Yes	Yes	No	Yes
Alaska	Yes	Yes	Partial	Yes	No	Yes	No
Arizona	Yes	Yes	Yes	No	No	No	Yes
Arkansas	No	Yes	Yes	Yes	Yes	No	No
California	Yes	No	Yes	Yes	No	Yes	Yes
Colorado	Yes	Yes	Yes	Yes	No	No	Yes
Connecticut	Yes	Yes	Yes	No	Yes	No	Yes
Delaware	Yes	Yes	Partial	No	Yes	No	Yes
Florida	Yes	Yes	Yes	No	Yes	Yes	Yes
Georgia	Yes	Yes	Yes	No	No	No	Yes
Hawaii	Yes	Yes	Yes	Yes	Yes	No	No
Idaho	Yes	Yes	Yes	Yes	Yes	No	Yes
Illinois	Yes	Yes	Yes	Yes	Yes	No	Yes
Indiana	Yes	Yes	Yes	Yes	No	No	Yes
Iowa	Yes	Yes	Partial	No	Yes	Yes	No
Kansas	Yes	Yes	Yes	Yes	No	No	No
Kentucky	Yes	Yes	Yes	No	No	No	No
Louisiana	Yes	Yes	Partial	No	Yes	No	No
Maine	Yes	Yes	Yes	Yes	Yes	Yes	No
Maryland	Yes	Yes	Yes	No	Yes	No	Yes
Massachusetts	Yes	Yes	Yes	Yes	No	No	Yes
Michigan	Yes	No	Yes	No	No	No	Yes
Minnesota	Yes	Yes	No	No	No	Yes	Yes
Mississippi	No	Yes	Yes	Yes	No	No	No
Missouri	Yes	Yes	Yes	Yes	Yes	No	Yes
Montana	Yes	Yes	Yes	Yes	No	No	Yes
Nebraska	Yes	Yes	Yes	No	Yes	No	No
Nevada	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
New Hampshire	Yes	Yes	Partial	Yes	No	No	Yes
New Jersey	Yes	Yes	Yes	No	No	No	No
New Mexico	Yes	Yes	Yes	Yes	Yes	No	No
New York	Yes	Yes	Yes	No	No	Yes	Yes
North Carolina	Yes	Yes	Partial	No	No	No	Yes
North Dakota	Yes	Yes	Yes	Yes	No	No	No
Ohio	Yes	Yes	Yes	No	Yes	No	No
Oklahoma	Yes	Yes	Yes	Yes	No	No	Yes
Oregon	Yes	Yes	No	Yes	No	No	Yes
Pennsylvania	Yes	Yes	Yes	No	No	No	Yes
Rhode Island	Yes	Yes	Yes	Yes	Yes	No	Yes
South Carolina	Yes	Yes	Yes	No	No	No	Yes
South Dakota	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Tennessee	Yes	Yes	Yes	No	Yes	No	Yes
Texas	Yes	Yes	Partial	Yes	Yes	No	Yes
Utah	Yes	Yes	Yes	Yes	No	No	Yes
Vermont	Yes	Yes	Yes	Yes	Yes	No	No
Virginia	Yes	Yes	Yes	No	No	No	Yes
Washington	No	No	No	No	No	No	Yes
West Virginia	Yes	Yes	Yes	No	No	No	Yes
Wisconsin	Yes	Yes	No	Yes	Yes	No	Yes
Wyoming	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
District of Columbia	No	Yes	Yes	Yes	Yes	No	Yes

Source: CCH.

Table 12
Individual Income Tax Rates
As of July 1, 2009

State	Federal Deductibility	Tax Rates and Brackets for Single Filers (a)	Standard Deduction		Personal Exemption (b)		Local Option Income Tax Rate (v)
			Single	Joint	Single	Dependents	
Alabama	Yes	2% > $0 4% > $500 5% > $3,000	$2,000	$4,000	$1,500	$300	0.19%
Alaska	No	None	n.a.	n.a.	n.a.	n.a.	None
Arizona	No	2.59% > $0 2.88% > $10,000 3.36% > $25,000 4.24% > $50,000 4.54% > $150,000	$4,502	$9,004	$2,100	$2,100	None
Arkansas (k)(r)	No	1% > $0 2.5% > $ 3,800 3.5% > $7,600 4.5% > $11,400 6% > $19,000 7% > 31,700	$2,000	$4,000	$22 (c)	$22 (c)	0.60%
California	No	1.25% > $0 2.5% > $3,800 4.5% > $16,994 6.5% > $26,821 8.25% > $37,233 9.55% > $47,055 10.55% > $1,000,000	$3,516	$7,032	$94 (c)	$294 (c)	None
Colorado	No	4.63% of federal taxable income	n.a.	n.a.	n.a.	n.a.	None
Connecticut	No	3% > $0 5% > $10,000	n.a.	n.a.	$13,000 (e)	n.a.	None
Delaware	No	2.2% > $2,000 3.9% > $5,000 4.8% > $10,000 5.2% > $20,000 5.55% > $25,000 6.95% > $60,000	$3,250	$6,500	$110 (c)	$110 (c)	0.16%
Florida	No	None	n.a.	n.a.	n.a.	n.a.	None
Georgia	No	1% > $0 2% > $750 3% > $2,250 4% > $3,750 5% > $5,200 6% > $7,000	$2,300	$3,000	$2,700	$3,000	None
Hawaii	No	1.4% > $0 3.2% > $2,400 5.5% > $4,800 6.4% > $9,600 6.8% > $14,400 7.2% > $19,200 7.6% > $24,000 7.9% > $36,000 8.25% > $48,000 9% > $150,000 10% > $175,000 11% > $200,000	$2,000	$4,000	$1,040	$1,040	None
Idaho	No	1.6% > $0 3.6% > $1,272 4.1% > $2,544 5.1% > $3,816 6.1% > $5,088 7.1% > $6,360 7.4% > $9,540 7.8% > $25,441	$5,450 (s)	$10,900 (s)	$ 1040 (s)	$1,040 (s)	None
Illinois	No	3% of federal adjusted gross income with modification	n.a.	n.a.	$2,000	$2,000	None

Table 12 (continued)
Individual Income Tax Rates
As of July 1, 2009

State	Federal Deductibility	Tax Rates and Brackets for Single Filers (a)	Standard Deduction		Personal Exemption (b)		Local Option Income Tax Rate (v)
			Single	Joint	Single	Dependents	
Indiana	No	3.4% of federal adjusted gross income with modification	n.a.	n.a.	$1,000	$1,000 (i)	1.16%
Iowa (r)	Yes	0.36% > $0 0.72% > $1,407 2.43% > $2,814 4.5% > $5,628 6.12% > $12,663 6.48% > $21,105 6.8% > $28,140 7.92% > 42,210 7.8% > $25,441	$1,750	$4,310	$40 (c)	$40 (c)	0.30%
Kansas	No	3..5% > $0 6.25% > $15,000 6.45% > $30,000	$5,450	$10,900	$2,250	$2,250	None
Kentucky	No	2% > $0 3% > $3,000 4% > $4,000 5% > $5,000 5.8% > $8,000 6% > $75,000	$2,050 (r)	$2,050 (r)	$20 (c)	$20 (c)	0.76%
Louisiana	Yes	2% > $0 4% > $12,500 6% > $50,000	n.a.	n.a.	$4,500 (l)	$1,000	None
Maine (r)	No	6.5% > $0 6.85% > $250,000	$5,450	$9,100	$2,850	$2,850	None
Maryland	No	2% > $0 3% > $1,000 4% > $2,000 4,75% > $3,000 5% > $150,000 5.25% > $300,000 5.5% > $500,000 6.25% > $1,00,000,000	$2,000 (m)	$4,000 (m)	$3,200	$3,200	2.98%
Massachusetts	No	5.3% and 12% (f)	n.a.	n.a.	$4,125	$4,125	None
Michigan	No	4.35% of federal adjusted gross income with modification	n.a.	n.a.	$3,400 (s)	$3,400 (s)	0.44%
Minnesota	No	5.35% > $0 4% > $5,000 5% > $10,000	$5,450 (s)	$10,900 (s)	$3,500 (s)	$3,500 (s)	None
Mississippi	No	3% > $0 4% > $5,000 5% > $10,000	$2,300	$4,600	$6,000	$1,500	None
Missouri	Limited	1.5% > $0 2% > $1,000 2.5% > $2,000 3% > $3,000 3.5% > $4,000 4% > $5,000 4.5% >$6,000 5% > $7,000 5.5% > $8,000 6% > $9,000	$5,450 (s)	$10,900 (s)	$2,100	$1,200	0.12%
Montana (r)	Limited	1% > $0 2% > $2,600 3% > $4,600 4% > $7,000 5% > $9,500 6% > $12,200 6.9% > $15,600	$3,810	$7,620	$2,040	$2,040	None

Table 12 (continued)
Individual Income Tax Rates
As of July 1, 2009

State	Federal Deductibility	Tax Rates and Brackets for Single Filers (a)	Standard Deduction		Personal Exemption (b)		Local Option Income Tax Rate (v)
			Single	Joint	Single	Dependents	
Nebraska	No	2.56% > $0 3.57% > $2,400 5.12% > $17,500 6.84% > $27,000	$5,450 (r)	$10,900 (r)	$106 (c)(n)	$106 (c)(n)	None
Nevada	No	None	n.a.	n.a.	n.a.	n.a.	None
New Hampshire	No	5% > $0 (h)	$2,400	$4,800	n.a.	n.a.	None
New Jersey	No	1.4% > $0 1.75% > $20,000 3.5% > $35,000 5.525% > $40,000 6.37% > $75,000 8% > $400,000 10.25% > $500,000 10.75% >$1,000,000	n.a.	n.a.	$1,000	$1,500	0.09%
New Mexico	No	1.7% > $0 3.2% > $5,500 4.7% > $11,000 4.9% > $16,000	$5,450 (s)	$10,900 (s)	$3,500 (s)	$3,500 (s)	None
New York	No	4% > $0 4.5% > $8,000 5.25% > $11,000 5.9% > $13,000 6.85% > $20,000 7.85% > $200,000 8.97% > $500,000	$7,500	$15,000	n.a.	$1,000	1.70%
North Carolina	No	6% > $0 7% > $12,750 7.75% > $60,000	$3,000	$6,000	$3,500	$3,500	None
North Dakota (r)	No	1.84% >$0 3.44% > $33,950 3.81% > $82,250 4.42% > $171,550 4.86% > $372,950	$5,450	$10,900	$3,500	$3,500	None
Ohio	No	0.587% > $0 1.174% > $5,000 2.348% > $10,000 2.935% > $15,000 3.521% > $20,000 4.109% > $40,000 4.695% > $80,000 5.451% > $100,000 5.925% > $200,000	n.a.	n.a.	$1,450 (r) +$20 (c)	$1,450 (r) +$20 (c)	1.82%
Oklahoma	No	0.5% > $0 1% > $1,000 2% > $2,500 3% > $3,750 4% > $4,900 5% > $7,200 5.5% > $8,700	$3,250	$6,500	$1,000	$1,000	None
Oregon (r)	Limited	5% > $0 7% > $3,050 9% > $7,600 10.8% > $125,000 11% > $250,000	$1,825	$3,650	$165 (c)(r)	$165 (c)(r)	0.36%
Pennsylvania	No	3.07% > $0	n.a.	n.a.	n.a.	n.a.	1.25%
Rhode Island (r)	No	3.75% > $0 7% > $33,950 7.75% > $82,250 9% > $171,550 9.9% > $372,950	$5,450	$8,900	$3,500	$3,500	None

Table 12 (continued)
Individual Income Tax Rates
As of July 1, 2009

State	Federal Deductibility	Tax Rates and Brackets for Single Filers (a)	Standard Deduction		Personal Exemption (b)		Local Option Income Tax Rate (v)
			Single	Joint	Single	Dependents	
South Carolina (r)	No	0% > $0 3% > $2,670 4% > $5,340 5% > $8,010 6% > $10,680 7% > $13,350	$5,450 (s)	$10,900 (s)	$3,500 (s)	$3,500 (s)	None
South Dakota	No	None	n.a.	n.a.	n.a.	n.a.	None
Tennessee	No	6% > $0 (h)	n.a.	n.a.	$1,250	n.a.	None
Texas	No	None	n.a.	n.a.	n.a.	n.a.	None
Utah	No	5.0% > $0	$5,450 (s)	$10,900 (s)	$2,650 (q)	$2,650 (q)	None
Vermont (r)	No	3.55% > $0 7% > $33,950 8.25% > $82,250 8.9% > $171,550 9.4% > $372,950	$5,450 (s)	$10,900 (s)	$3,500 (s)	$3,500 (s)	None
Virginia	No	2% > $0 3% > $3,000 5% > $5,000 5.75% > $17,000	$3,000	$6,000	$930	$930	None
Washington	No	None	n.a.	n.a.	n.a.	n.a.	None
West Virginia	No	3% > $0 4% > $10,000 4.5% > $25,000 6% > $40,000 6.5% > $60,000	n.a.	n.a.	$2,000	$2,000	None
Wisconsin (r)	No	4.6% > $10,2220 6.15% > $10,220 6.5% > $20,440 6.75% > $153,280 7.75% > $225,000	$8,790 (j)	$15,830 (j)	$700	$700	None
Wyoming	No	None	n.a.	n.a.	n.a.	n.a.	None
District of Columbia	No	4% > $0 6% > $10,000 8.5% > $40,000	$4,000	$4,000	$1,670	$1,670	n.a.

(a) Applies to single taxpayers and married people filing separately. Most states double brackets for married filing joint.

(b) Married-joint filers generally receive double the single exemption

(c) Tax credit

(e) Maximum equals $13,000. Value Decreases as income increases.

(f) The 12% rate applies to short-term capital gains, long - and short-term capital gains on collectibles and pre - 1996 installment sales classified as capital gain income for Massachusetts purposes.

(h) Applies to interest and dividend income only

(i) Additional $1,500 dependent child exemption

(j) Deduction phases out to zero for single filers at $80,000 and joint filers at $90,895

(k) Rates apply to regular tax table. A special tax table is available for low-income taxpayers that reduce their tax payments.

(l) Standard deduction and personal exemptions are combined: $,500 for single and married filing separately; $9,000 married filing jointly and heard of household

(m) The standard deduction is 15 percent of income with a minimum of $1,500 and a cap of $2,000 for single filers, married filing separately filers and dependent filers earning more than $13,333. The standard deduction is capped at $4,000 for married filing jointly filers, head of household filers and qualifying widowers earning more than $26,667.

(n) The $106 personal exmption credit is phased out for filers with adjusted gross income of $73,000 or more.

(q) Three-forths federal exemption.

(r) Indexes for inflation

(s) Deductions and exemptions tied to federal tax system. Federal deductions and exemptions are indexed for inflation.

(v) Weighted average of rates in counties and large municipalities.

Source: Tax Foundation, state tax forms and instructions and CCH

Table 13
Individual Income Tax Base Criteria
As of July 1, 2009

State	Marriage Penalty	Allow Filing Separately on a Single Return	Double Taxation			Indexation		
			Interest	Dividends	Capital Gains	Brackets	Standard Deduction	Exemption
Alabama	No	No	Yes	Yes	Yes	No	No	No
Alaska	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Arizona	No	No	Yes	Yes	Yes	No	Yes	No
Arkansas	No	Yes	Yes	Yes	Yes	Yes	No	Yes
California	Yes	No	Yes	Yes	Yes	Yes	Yes	Yes
Colorado	Yes	No	Yes	Yes	Yes	Yes	Yes	Yes
Connecticut	Yes	No	Yes	Yes	Yes	No	No	No
Delaware	Yes	Yes	Yes	Yes	Yes	No	Yes	No
Florida	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Georgia	Yes	No	Yes	Yes	Yes	No	No	No
Hawaii	No	No	Yes	Yes	Yes	No	No	No
Idaho	No	No	Yes	Yes	Yes	Yes	Yes	Yes
Illinois	No	No	Yes	Yes	Yes	Yes	Yes	No
Indiana	No	No	Yes	Yes	Yes	Yes	Yes	No
Iowa	Yes	Yes	Yes	Yes	Yes	Yes	Yes	No
Kansas	No	No	Yes	Yes	Yes	No	Yes	No
Kentucky	Yes	Yes	Yes	Yes	Yes	No	Yes	No
Louisiana	No	No	Yes	Yes	Yes	No	No	Yes
Maine	Yes	No	Yes	Yes	Yes	Yes	Yes	No
Maryland	Yes	No	Yes	Yes	Yes	No	No	No
Massachusetts	No	No	Yes	Yes	Yes	Yes	Yes	Yes
Michigan	No	No	Yes	Yes	Yes	Yes	Yes	Yes
Minnesota	Yes	No	Yes	Yes	Yes	Yes	Yes	Yes
Mississippi	Yes	Yes	Yes	Yes	Yes	No	No	No
Missouri	Yes	Yes	Yes	Yes	Yes	No	Yes	No
Montana	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Nebraska	No	No	Yes	Yes	Yes	No	Yes	Yes
Nevada	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
New Hampshire	No	No	Yes	No	Yes	Yes	No	No
New Jersey	Yes	No	Yes	Yes	Yes	No	Yes	No
New Mexico	Yes	No	Yes	Yes	Yes	No	Yes	Yes
New York	Yes	No	Yes	Yes	Yes	No	No	No
North Carolina	Yes	No	Yes	Yes	Yes	No	No	Yes
North Dakota	Yes	No	Yes	Yes	Yes	Yes	Yes	Yes
Ohio	Yes	No	Yes	Yes	Yes	No	No	Yes
Oklahoma	Yes	No	Yes	Yes	Yes	No	Yes	No
Oregon	Yes	No	Yes	Yes	Yes	Yes	Yes	Yes
Pennsylvania	No	No	Yes	Yes	Yes	Yes	Yes	Yes
Rhode Island	Yes	No	Yes	Yes	Yes	Yes	Yes	Yes
South Carolina	Yes	No	Yes	Yes	Yes	Yes	Yes	Yes
South Dakota	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Tennessee	No	No	Yes	Yes	No	Yes	Yes	No
Texas	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Utah	Yes	No	Yes	Yes	Yes	Yes	Yes	Yes
Vermont	Yes	No	Yes	Yes	Yes	Yes	Yes	Yes
Virginia	Yes	No	Yes	Yes	Yes	No	No	No
Washington	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
West Virginia	Yes	No	Yes	Yes	Yes	No	No	No
Wisconsin	Yes	No	Yes	Yes	Yes	Yes	Yes	No
Wyoming	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Dist. of Columbia	Yes	Yes	Yes	Yes	Yes	No	Yes	Yes

Sources: CCH, Tax Foundation.

Table 14
Other Individual Income Tax Base Criteria
As of July 1, 2009

State	Federal Income Used as State Tax Base	State Tax Deductible	AMT Levied	Recognition of LLC Status	Recognition of S-Corp Status
Alabama	No	Yes	No	Yes	Yes
Alaska	n.a.	n.a.	n.a.	Yes	Yes
Arizona	Yes	Yes	No	Yes	Yes
Arkansas	No	Yes	No	Yes	Yes
California	Yes	Yes	Yes	Yes	Partial
Colorado	Yes	Yes	Yes	Yes	Yes
Connecticut	Yes	Yes	Yes	Yes	Yes
Delaware	Yes	Yes	No	Yes	Yes
Florida	n.a.	n.a.	n.a.	Yes	Yes
Georgia	Yes	Yes	No	Yes	Yes
Hawaii	Yes	Yes	No	Yes	Yes
Idaho	Yes	Yes	No	Yes	Yes
Illinois	Yes	Yes	No	Yes	Partial
Indiana	Yes	Yes	No	Yes	Yes
Iowa	No	Yes	Yes	Yes	Yes
Kansas	Yes	Yes	No	Yes	Yes
Kentucky	Yes	Yes	No	Yes	Yes
Louisiana	Yes	Yes	No	Yes	No
Maine	Yes	Yes	Yes	Yes	Yes
Maryland	Yes	Yes	No	Yes	Yes
Massachusetts	Yes	Yes	No	Yes	Partial
Michigan	Yes	Yes	No	Yes	No
Minnesota	Yes	Yes	Yes	Yes	Yes
Mississippi	No	Yes	No	Yes	Yes
Missouri	Yes	Yes	No	Yes	Yes
Montana	Yes	Yes	No	Yes	Yes
Nebraska	Yes	Yes	Yes	Yes	Yes
Nevada	n.a.	n.a.	n.a.	n.a.	n.a.
New Hampshire	No	Yes	No	Partial	No
New Jersey	No	Yes	No	Partial	Yes
New Mexico	Yes	Yes	No	Yes	Yes
New York	Yes	Yes	Yes	Yes	Partial
North Carolina	Yes	Yes	No	Yes	Yes
North Dakota	Yes	Yes	No	Yes	Yes
Ohio	Yes	Yes	No	Partial	Yes
Oklahoma	Yes	Yes	No	Yes	Yes
Oregon	Yes	Yes	No	Yes	Yes
Pennsylvania	No	Yes	No	Yes	Yes
Rhode Island	Yes	Yes	Yes	Yes	Partial
South Carolina	Yes	Yes	No	Yes	Yes
South Dakota	n.a.	n.a.	n.a.	n.a.	n.a.
Tennessee	No	Yes	No	Yes	No
Texas	n.a.	n.a.	n.a.	No	No
Utah	Yes	Yes	No	Yes	Yes
Vermont	Yes	Yes	No	Yes	Yes
Virginia	Yes	Yes	No	Partial	Yes
Washington	n.a.	n.a.	n.a.	Yes	Yes
West Virginia	Yes	Yes	Yes	Yes	Yes
Wisconsin	Yes	Yes	Yes	Yes	Yes
Wyoming	n.a.	n.a.	n.a.	n.a.	n.a.
Dist. of Columbia	Yes	Yes	No	Yes	No

Sources: CCH, Tax Foundation.

Table 15
Sales and Excise Tax Rates
As of July 1, 2009

State	State Sales Tax Rate	County and City Sales Tax: Weighted Average Rate	County and City Sales Tax: Are Localities Permitted to Define Tax Base?	Selective Sales Taxes (Excise Taxes): Gasoline Tax (cents per gallon)	Diesel Tax (cents per gallon)	Cigarette Tax (cents per pack of 20)	Beer Tax (per gallon)	Spirits Tax (per gallon)
Alabama	4.00 %	2.27%	Yes	21.2¢	22.2¢	42.5¢	$ 1.05	$ 18.87 (a)
Alaska	None	0.86	Yes	8.0	8.0	200.0	1.07	12.80
Arizona	5.60	2.30	Yes	19.0	28.0	200.0	0.16	3.00
Arkansas	6.00	1.87	Yes	21.8	22.8	115.0	0.21	2.58
California	8.25	0.81	Yes	19.2	19.2	87.0	0.20	3.30
Colorado	2.90%	4.21%	Yes	22.0¢	20.5¢	84.0¢	$ 0.08	$ 2.28
Connecticut	6.00	None	Yes	25.0	43.4	200.0	0.20	4.50
Delaware	None	None	No	23.0	22.0	115.0	0.16	3.75
Florida	6.00	1.01	Yes	33.2	29.0	133.9	0.48	6.50
Georgia	4.00	2.97	Yes	7.5	7.5	37.0	1.01	3.79
Hawaii	4.00%	0.35%	No	32.6¢	32.6¢	260.0¢	$ 0.93	$ 5.95
Idaho	6.00	None	Yes	25.0	25.0	57.0	0.15	10.96 (a)
Illinois	6.25	2.01	Yes	20.9	23.4	98.0	0.19	8.55
Indiana	7.00	None	Yes	19.0	28.0	99.5	0.12	2.68
Iowa	6.00	0.98	Yes	22.0	23.5	136.0	0.19	12.47
Kansas	5.30%	1.57%	Yes	25.0¢	27.0¢	79.0¢	$ 0.18	$ 2.50
Kentucky	6.00	None	No	22.5	19.5	60.0	0.10	6.46
Louisiana	4.00	4.46	Yes	20.0	20.0	36.0	0.32	2.50
Maine	5.00	None	No	29.9	30.3	200.0	0.35	5.21 (a)
Maryland	6.00	None	Yes	23.5	24.3	200.0	0.09	1.50
Massachusetts	6.25%	None	Yes	23.5¢	23.5¢	251.0¢	$ 0.11	$ 4.04
Michigan	6.00	None	No	19.9	15.9	200.0	0.20	10.91
Minnesota	6.88	0.28%	Yes	22.0	22.0	150.4	0.15	5.08
Mississippi	7.00	None	Yes	18.8	18.8	68.0	0.43	6.75 (a)
Missouri	4.23	2.78	Yes	17.6	17.6	17.0	0.06	2.00
Montana	None	None	No	27.8¢	28.6¢	170.0¢	$ 0.14	$ 8.62 (a)
Nebraska	5.50%	0.92%	No	26.9	26.3	64.0	0.31	3.75
Nevada	6.85	0.74	Yes	32.6	28.6	80.0	0.16	3.60
New Hampshire	None	None	No	19.6	19.6	178.0	0.30	(b)
New Jersey	7.00	None	Yes	14.5	17.5	270.0	0.12	5.50
New Mexico	5.00%	1.37%	Yes	18.0¢	19.0¢	91.0¢	$ 0.41	$ 6.06
New York	4.00	4.25	No	33.2	31.4	275.0	0.11	6.44
North Carolina	4.25	2.32	Yes	30.2	30.2	35.0	0.53	13.39 (a)
North Dakota	5.00	0.96	Yes	23.0	23.0	44.0	0.16	2.50
Ohio	5.50	1.31	Yes	28.0	28.0	125.0	0.18	9.04 (a)
Oklahoma	4.50%	3.92%	Yes	17.0¢	14.0¢	103.0¢	$ 0.40	$ 5.56
Oregon	None	None	Yes	25.0	24.3	118.0	0.08	24.63 (a)
Pennsylvania	6.00	0.21	No	32.3	39.2	135.0	0.08	6.54 (a)
Rhode Island	7.00	None	Yes	31.0	31.0	346.0	0.11	3.75
South Carolina	6.00	1.05	Yes	16.8	16.8	7.0	0.77	4.97
South Dakota	4.00%	1.48%	Yes	22.0¢	24.0¢	153.0¢	$ 0.27	$ 3.93
Tennessee	7.00	2.42	Yes	21.4	18.4	62.0	0.14	4.46
Texas	6.25	1.32	Yes	20.0	20.0	141.0	0.20	2.40
Utah	5.95	0.62	Yes	24.5	24.5	69.5	0.41	11.41 (a)
Vermont	6.00	None	Yes	20.0	26.0	224.0	0.27	0.68 (b)
Virginia	5.00%	None	Yes	18.1¢	19.6¢	30.0¢	$ 0.26	$ 20.13 (a)
Washington	6.50	2.15%	Yes	37.5	37.5	202.5	0.26	26.45 (a)
West Virginia	6.00	None	Yes	32.2	32.2	55.0	0.18	1.85 (a)
Wisconsin	5.00	0.43	Yes	32.9	32.9	252.0	0.06	3.25
Wyoming	4.00	1.37	Yes	14.0	14.0	60.0	0.02	(b)
Dist. of Columbia	5.75%	None	No	20.0¢	20.0¢	200.0¢	$ 0.09	$ 1.50

(a) Eighteen states outlaw private liquor sales and set up state-run stores. These are called “control states” while “license states” are those that permit private wholesale and retail sales. All license states have an excise tax rate in law, expressed in dollars per gallon. Control states levy no statutory tax but usually raise comparable revenue by charging higher prices. Since July 2005, the Distilled Spirits Council of the U.S., a trade association, has computed approximate excise tax rates for control states by comparing prices of typical products sold in their state-run stores to the pre-tax prices of liquor in states where liquor is privately sold.

(b) In New Hampshire, Vermont and Wyoming, average liquor prices charege in state-run stores are lower than pre-tax prices in license states.
Source: CCH, American Petroleum Institute, Distilled Spirits Council of the U.S., and Tax Foundation.

Table 16
State Sales Tax Exemptions for Business-to-Business Transactions
As of July 1, 2009

State	Insecticides and Pesticides	Fertilizer, Seed and Feed	Seedlings, Plants and Shoots	Manufacturing Machinery	Utilities	Farm Machinery
Alabama	Exempt	Exempt	Exempt	Taxable	Taxable	Taxable
Arizona	Taxable	Taxable	Exempt	Exempt	Taxable	Exempt
Arkansas	Taxable	Exempt	Exempt	Taxable	Taxable	Exempt
California	Exempt	Exempt	Exempt	Taxable	Exempt	Taxable
Colorado	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
Connecticut	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
Florida	Taxable	Exempt	Exempt	Taxable	Exempt	Exempt
Georgia	Taxable	Exempt	Exempt	Exempt	Taxable	Exempt
Hawaii	Exempt	Taxable	Taxable	Taxable	Taxable	Taxable
Idaho	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
Illinois	Taxable	Exempt	Exempt	Exempt	Taxable	Exempt
Indiana	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
Iowa	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
Kansas	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
Kentucky	Taxable	Exempt	Exempt	Taxable	Exempt	Exempt
Louisiana	Taxable	Exempt	Exempt	Taxable	Taxable	Taxable
Maine	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
Maryland	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
Massachusetts	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
Michigan	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
Minnesota	Taxable	Exempt	Exempt	Taxable	Exempt	Exempt
Mississippi	Taxable	Exempt	Exempt	Taxable	Taxable	Taxable
Missouri	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
Nebraska	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
Nevada	Exempt	Exempt	Exempt	Taxable	Taxable	Exempt
New Jersey	Taxable	Exempt	Exempt	Exempt	Taxable	Exempt
New Mexico	Taxable	Exempt	Exempt	Taxable	Taxable	Taxable
New York	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
North Carolina	Taxable	Exempt	Exempt	Taxable	Taxable	Exempt
North Dakota	Taxable	Exempt	Exempt	Taxable	Taxable	Taxable
Ohio	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
Oklahoma	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
Pennsylvania	Taxable	Exempt	Exempt	Exempt	Taxable	Exempt
Rhode Island	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
South Carolina	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
South Dakota	Taxable	Exempt	Exempt	Taxable	Taxable	Taxable
Tennessee	Taxable	Exempt	Exempt	Exempt	Taxable	Exempt
Texas	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
Utah	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
Vermont	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
Virginia	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
Washington	Taxable	Exempt	Exempt	Exempt	Taxable	Taxable
West Virginia	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
Wisconsin	Taxable	Exempt	Exempt	Exempt	Exempt	Exempt
Wyoming	Exempt	Exempt	Exempt	Exempt	Exempt	Taxable
Dist. of Columbia	Exempt	Taxable	Taxable	Taxable	Exempt	Taxable

Note: States with no state sales tax omitted from table: Alaska, Delaware, Montana, New Hampshire and Oregon.
Sources: CCH, Tax Foundation.

Table 16 (continued)
State Sales Tax Exemptions for Business-to-Business Transactions
As of July 1, 2009

State	General Treatment of Services	Cleaning Services	Transportation Services	Repair Services	Professional and Personal Services	Custom Software
Alabama	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Arizona	Many Taxable	Exempt	Taxable	Exempt	Exempt	Exempt
Arkansas	Many Taxable	Taxable	Exempt	Taxable	Exempt	Taxable
California	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Colorado	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Connecticut	Many Taxable	Taxable	Exempt	Taxable	Taxable	Taxable
Florida	Many Taxable	Taxable	Exempt	Exempt	Exempt	Exempt
Georgia	Exempt	Exempt	Taxable	Exempt	Exempt	Exempt
Hawaii	Taxable	Taxable	Taxable	Taxable	Taxable	Taxable
Idaho	Exempt	Exempt	Taxable	Exempt	Exempt	Exempt
Illinois	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Indiana	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Iowa	Many Taxable	Taxable	Exempt	Taxable	Taxable	Exempt
Kansas	Many Taxable	Exempt	Exempt	Taxable	Exempt	Exempt
Kentucky	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Louisiana	Exempt	Exempt	Exempt	Taxable	Exempt	Exempt
Maine	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Maryland	Exempt	Taxable	Exempt	Exempt	Exempt	Exempt
Massachusetts	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Michigan	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Minnesota	Many Taxable	Taxable	Exempt	Exempt	Exempt	Exempt
Mississippi	Taxable	Exempt	Exempt	Taxable	Exempt	Taxable
Missouri	Exempt	Exempt	Taxable	Exempt	Exempt	Exempt
Nebraska	Exempt	Taxable	Exempt	Taxable	Exempt	Taxable
Nevada	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
New Jersey	Many Taxable	Taxable	Exempt	Taxable	Exempt	Exempt
New Mexico	Taxable	Taxable	Taxable	Taxable	Taxable	Taxable
New York	Many Taxable	Taxable	Exempt	Taxable	Exempt	Exempt
North Carolina	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
North Dakota	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Ohio	Many Taxable	Taxable	Taxable	Taxable	Exempt	Taxable
Oklahoma	Many Taxable	Exempt	Taxable	Exempt	Exempt	Exempt
Pennsylvania	Many Taxable	Taxable	Exempt	Taxable	Exempt	Exempt
Rhode Island	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
South Carolina	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
South Dakota	Taxable	Taxable	Taxable	Taxable	Taxable	Taxable
Tennessee	Exempt	Exempt	Exempt	Taxable	Exempt	Taxable
Texas	Many Taxable	Taxable	Exempt	Taxable	Taxable	Taxable
Utah	Many Taxable	Exempt	Taxable	Taxable	Exempt	Exempt
Vermont	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Virginia	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Washington	Many Taxable	Exempt	Exempt	Taxable	Exempt	Exempt
West Virginia	Taxable	Taxable	Taxable	Taxable	Exempt	Taxable
Wisconsin	Many Taxable	Exempt	Exempt	Taxable	Exempt	Exempt
Wyoming	Exempt	Exempt	Taxable	Taxable	Exempt	Exempt
Dist. of Columbia	Many Taxable	Taxable	Exempt	Taxable	Exempt	Taxable

Note: States with no state sales tax omitted from table: Alaska, Delaware, Montana, New Hampshire and Oregon.
Source: CCH.

Table 16 (continued)
State Sales Tax Exemptions for Business-to-Business Transactions
As of July 1, 2009

State	Modified Canned Software	Downloaded Software	Leasing Motor Vehicles	Leasing Tangible Personal Property	Leasing Rooms and Lodgings
Alabama	Taxable	Taxable	Taxable	Taxable	Taxable
Arizona	Taxable	Taxable	Taxable	Taxable	Taxable
Arkansas	Taxable	Exempt	Taxable	Taxable	Taxable
California	Taxable	Exempt	Taxable	Taxable	Exempt
Colorado	Exempt	Exempt	Taxable	Taxable	Taxable
Connecticut	Taxable	Taxable	Taxable	Taxable	Taxable
Florida	Exempt	Exempt	Taxable	Taxable	Taxable
Georgia	Taxable	Exempt	Taxable	Taxable	Taxable
Hawaii	Taxable	Taxable	Taxable	Taxable	Taxable
Idaho	Taxable	Taxable	Taxable	Taxable	Taxable
Illinois	Exempt	Taxable	Taxable	Exempt	Taxable
Indiana	Taxable	Taxable	Taxable	Taxable	Taxable
Iowa	Taxable	Exempt	Taxable	Taxable	Taxable
Kansas	Taxable	Taxable	Taxable	Taxable	Taxable
Kentucky	Exempt	Taxable	Exempt	Taxable	Taxable
Louisiana	Taxable	Taxable	Taxable	Taxable	Taxable
Maine	Taxable	Taxable	Taxable	Taxable	Taxable
Maryland	Exempt	Exempt	Taxable	Taxable	Taxable
Massachusetts	Exempt	Taxable	Taxable	Taxable	Taxable
Michigan	Taxable	Taxable	Taxable	Taxable	Taxable
Minnesota	Taxable	Taxable	Taxable	Taxable	Taxable
Mississippi	Taxable	Taxable	Taxable	Taxable	Taxable
Missouri	Exempt	Exempt	Taxable	Taxable	Taxable
Nebraska	Taxable	Taxable	Taxable	Taxable	Taxable
Nevada	Taxable	Exempt	Taxable	Taxable	Exempt
New Jersey	Taxable	Exempt	Taxable	Taxable	Taxable
New Mexico	Taxable	Taxable	Taxable	Taxable	Taxable
New York	Taxable	Taxable	Taxable	Taxable	Taxable
North Carolina	Taxable	Exempt	Exempt	Taxable	Taxable
North Dakota	Taxable	Taxable	Exempt	Taxable	Taxable
Ohio	Taxable	Taxable	Taxable	Taxable	Taxable
Oklahoma	Taxable	Exempt	Taxable	Taxable	Taxable
Pennsylvania	Taxable	Taxable	Taxable	Taxable	Taxable
Rhode Island	Taxable	Exempt	Taxable	Taxable	Taxable
South Carolina	Taxable	Exempt	Taxable	Taxable	Taxable
South Dakota	Taxable	Taxable	Taxable	Taxable	Taxable
Tennessee	Taxable	Taxable	Taxable	Taxable	Taxable
Texas	Taxable	Taxable	Exempt	Taxable	Taxable
Utah	Taxable	Taxable	Taxable	Taxable	Taxable
Vermont	Exempt	Exempt	Exempt	Taxable	Taxable
Virginia	Taxable	Exempt	Exempt	Taxable	Taxable
Washington	Exempt	Taxable	Taxable	Taxable	Taxable
West Virginia	Taxable	Taxable	Taxable	Taxable	Taxable
Wisconsin	Taxable	Taxable	Taxable	Taxable	Taxable
Wyoming	Taxable	Taxable	Taxable	Taxable	Taxable
Dist. of Columbia	Taxable	Taxable	Taxable	Taxable	Taxable

Note: States with no state sales tax omitted from table: Alaska, Delaware, Montana, New Hampshire and Oregon.
(a) Tax phases out completely in 2009. Current score reflects partial phase-out as of July 1, 2008.
Source: CCH.

Table 16 (continued)
State Sales Tax Exemptions for Business-to-Business Transactions As of July 1, 2009

State	Raw Material	Office Equipment	Pollution Control Equipment	
			Air	Water
Alabama	Exempt	Taxable	Exempt	Exempt
Arizona	Exempt	Taxable	Exempt	Exempt
Arkansas	Exempt	Taxable	Exempt	Exempt
California	Exempt	Taxable	Taxable	Taxable
Colorado	Exempt	Taxable	Taxable	Taxable
Connecticut	Exempt	Taxable	Exempt	Exempt
Florida	Exempt	Taxable	Exempt	Exempt
Georgia	Exempt	Taxable	Exempt	Exempt
Hawaii	Taxable	Taxable	Exempt	Taxable
Idaho	Exempt	Taxable	Exempt	Exempt
Illinois	Exempt	Taxable	Taxable	Taxable
Indiana	Exempt	Taxable	Exempt	Exempt
Iowa	Exempt	Taxable	Exempt	Exempt
Kansas	Exempt	Taxable	Exempt	Exempt
Kentucky	Exempt	Taxable	Exempt	Exempt
Louisiana	Exempt	Taxable	Exempt	Exempt
Maine	Exempt	Taxable	Exempt	Exempt
Maryland	Exempt	Taxable	Exempt	Exempt
Massachusetts	Exempt	Taxable	Taxable	Taxable
Michigan	Exempt	Taxable	Exempt	Exempt
Minnesota	Exempt	Taxable	Taxable	Taxable
Mississippi	Exempt	Taxable	Exempt	Exempt
Missouri	Exempt	Taxable	Exempt	Exempt
Nebraska	Exempt	Taxable	Taxable	Taxable
Nevada	Exempt	Taxable	Taxable	Taxable
New Jersey	Exempt	Taxable	Taxable	Taxable
New Mexico	Exempt	Taxable	Taxable	Taxable
New York	Exempt	Taxable	Exempt	Exempt
North Carolina	Exempt	Taxable	Taxable	Taxable
North Dakota	Exempt	Taxable	Taxable	Taxable
Ohio	Exempt	Taxable	Exempt	Exempt
Oklahoma	Exempt	Taxable	Taxable	Taxable
Pennsylvania	Exempt	Taxable	Exempt	Exempt
Rhode Island	Exempt	Taxable	Exempt	Exempt
South Carolina	Exempt	Taxable	Exempt	Exempt
South Dakota	Exempt	Taxable	Taxable	Taxable
Tennessee	Exempt	Taxable	Exempt	Exempt
Texas	Exempt	Taxable	Exempt	Exempt
Utah	Exempt	Taxable	Exempt	Exempt
Vermont	Exempt	Taxable	Taxable	Taxable
Virginia	Exempt	Taxable	Exempt	Exempt
Washington	Exempt	Taxable	Taxable	Taxable
West Virginia	Exempt	Taxable	Exempt	Exempt
Wisconsin	Exempt	Taxable	Taxable	Taxable
Wyoming	Exempt	Taxable	Taxable	Taxable
Dist. of Columbia	Exempt	Taxable	Taxable	Taxable

Note: States with no state sales tax omitted from table: Alaska, Delaware, Montana, New Hampshire and Oregon.
Sources: CCH.

Table 17
State Sales Tax Exemptions for Business-to-Consumer Transactions As of July 1, 2009

State	Gasoline Exemption	Grocery Exemption
Alabama	Exempt	Taxable
Arizona	Exempt	Exempt
Arkansas	Exempt	Partial
California	Taxable	Exempt
Colorado	Partial	Exempt
Connecticut	Exempt	Exempt
Florida	Exempt	Exempt
Georgia	Partial	Exempt
Hawaii	Exempt	Taxable
Idaho	Exempt	Taxable
Illinois	Taxable	Partial
Indiana	Taxable	Exempt
Iowa	Exempt	Exempt
Kansas	Exempt	Taxable
Kentucky	Exempt	Exempt
Louisiana	Exempt	Exempt
Maine	Exempt	Exempt
Maryland	Exempt	Exempt
Massachusetts	Exempt	Exempt
Michigan	Taxable	Exempt
Minnesota	Exempt	Exempt
Mississippi	Exempt	Taxable
Missouri	Exempt	Partial
Nebraska	Exempt	Exempt
Nevada	Exempt	Exempt
New Jersey	Exempt	Exempt
New Mexico	Exempt	Exempt
New York	Partial	Exempt
North Carolina	Exempt	Exempt
North Dakota	Exempt	Exempt
Ohio	Exempt	Exempt
Oklahoma	Exempt	Taxable
Pennsylvania	Exempt	Exempt
Rhode Island	Exempt	Exempt
South Carolina	Exempt	Taxable
South Dakota	Exempt	Taxable
Tennessee	Exempt	Partial
Texas	Exempt	Exempt
Utah	Exempt	Partial
Vermont	Exempt	Exempt
Virginia	Exempt	Partial
Washington	Exempt	Exempt
West Virginia	Exempt	Partial
Wisconsin	Exempt	Exempt
Wyoming	Exempt	Exempt
District of Columbia	Exempt	Exempt

Note: States with no state sales tax omitted from table: Alaska, Delaware, Montana, New Hampshire and Oregon.
Sources: CCH, Tax Foundation, American Petroleum Institute.

Table 18
State Unemployment Insurance Tax Rates

State	Rates in Effect on July 1, 2009			Most Favorable Schedule		Least Favorable Schedule	
	Minimum Rate	Maximum Rate	Taxable Wage Threshold	Minimum Rate	Maximum Rate	Minimum Rate	Maximum Rate
Alabama	0.44%	6.04%	$ 8,000	0.20%	5.40%	0.65%	6.80%
Alaska	1.00	5.40	32,700	0.00	5.40	1.00	5.40
Arizona	0.02	5.40	7,000	0.02	5.40	0.10	5.40
Arkansas	0.90	6.80	10,000	0.00	5.90	0.90	6.80
California	1.50	6.20	7,000	0.10	5.40	1.50	6.20
Colorado	0.00%	5.40%	$ 10,000	0.00%	5.40%	1.00%	5.40%
Connecticut	1.90	6.80	15,000	0.50	5.40	1.90	6.80
Delaware	1.00	8.00	10,500	0.10	8.00	0.10	8.00
Florida	0.12	5.40	7,000	0.10	5.40	0.10	5.40
Georgia	0.03	5.40	8,500	0.01	5.40	0.03	7.29
Hawaii	0.00%	5.40%	$ 13,000	0.00%	5.40%	2.40%	5.40%
Idaho	0.45	5.40	33,200	0.18	5.40	0.96	6.80
Illinois	0.60	5.80	12,300	0.20	6.40	0.30	9.60
Indiana	1.10	5.60	7,000	0.10	5.40	1.10	5.60
Iowa	0.00	8.00	23,700	0.00	7.00	0.00	9.00
Kansas	0.00%	7.40%	$ 8,000	0.00%	7.40%	0.01%	7.40%
Kentucky	1.00	10.00	8,000	0.30	9.00	1.00	10.00
Louisiana	0.10	6.20	7,000	0.09	6.00	0.30	6.00
Maine	0.44	5.40	12,000	0.42	5.40	1.03	8.89
Maryland	0.60	9.00	8,500	0.30	7.50	2.20	13.50
Massachusetts	1.26%	12.27%	$ 14,000	0.80%	7.80%	1.58%	15.40%
Michigan	0.06	10.30	9,000	0.06	10.30	0.06	10.30
Minnesota	0.56	10.70	26,000	0.10	9.00	0.40	9.30
Mississippi	0.70	5.40	7,000	0.10	5.40	0.10	5.40
Missouri	0.00	9.75	12,500	0.00	5.40	0.00	7.80
Montana	0.00%	6.12%	$ 25,100	0.00%	6.12%	1.62%	6.12%
Nebraska	0.00	5.40	9,000	0.00	5.40	0.70	5.40
Nevada	0.25	5.40	26,600	0.25	5.40	0.25	5.40
New Hampshire	0.10	6.50	8,000	0.10	6.50	0.10	6.30
New Jersey	0.30	5.40	28,900	0.18	5.40	1.18	7.70
New Mexico	0.03%	5.40%	$ 20,900	0.03%	5.40%	2.70%	5.40%
New York	0.70	8.70	8,500	0.00	5.90	0.90	8.90
North Carolina	0.00	6.84	19,300	0.00	5.70	0.00	5.70
North Dakota	0.20	9.86	23,700	0.01	8.09	0.01	10.09
Ohio	0.30	9.00	9,000	0.00	6.30	0.30	9.00
Oklahoma	0.10%	5.50%	$ 14,200	0.20%	5.50%	0.50%	5.50%
Oregon	0.90	5.40	31,300	0.50	5.40	2.20	5.40
Pennsylvania	1.84	13.15	8,000	0.30	7.70	0.30	7.70
Rhode Island	1.69	9.79	18,000	0.60	7.00	1.90	10.00
South Carolina	1.14	6.00	7,000	0.54	5.40	1.24	6.10
South Dakota	0.00%	8.50%	$ 10,000	0.00%	8.50%	1.50%	10.00%
Tennessee	0.50	10.00	7,000	0.00	10.00	0.50	10.00
Texas	0.26	6.26	9,000	0.00	6.00	0.00	6.00
Utah	0.20	9.20	27,800	0.00	9.00	0.00	9.00
Vermont	0.80	6.50	8,000	0.40	5.40	1.30	8.40
Virginia	0.18%	6.28%	$ 22,100	0.00%	5.40%	0.10%	6.20%
Washington	0.00	5.40	35,700	0.00	5.40	0.00	5.40
West Virginia	1.50	7.50	12,000	0.00	8.50	1.50	8.50
Wisconsin	0.00	8.50	12,000	0.00	8.90	0.70	8.50
Wyoming	0.30	9.10	21,500	0.00	10.00	0.00	10.00
District of Columbia	1.30%	6.60%	$ 9,000	0.10%	5.40%	1.90%	7.40%

Source: U.S. Department of Labor.

Table 19
State Unemployment Insurance Tax Base Criteria
As of January 1, 2009

State	State Experience Formula	Benefits are Charged to Employers in Proportion to Base Period Wages	Company Charged for Benefits If					
			Employee's Benefit Award Reversed	Reimbursements on Combined Wage Claims	Employee Left Voluntarily	Employee Discharged for Misconduct	Employee Refused Suitable Work	Employee Continues to Work for Employer Part-time
Alabama	Benefit-Ratio	Yes	No	Yes	No	No	Yes	No
Alaska	Payroll Variation	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Arizona	Reserve-Ratio	No	No	No	No	No	Yes	No
Arkansas	Reserve-Ratio	Yes	Yes	Yes	No	No	Yes	No
California	Reserve-Ratio	Yes	No	Yes	No	No	No	No
Colorado	Reserve-Ratio	No (b)	No	No	No	No	Yes	Yes
Connecticut	Benefit-Ratio	Yes	Yes	Yes	No	No	No	Yes
Delaware	State Experience	Yes	No	No	No	No	No	No
Florida	Benefit-Ratio	Yes	No	Yes	No	No	Yes	Yes
Georgia	Reserve-Ratio	No (a)	No	No	No	No	Yes	Yes
Hawaii	Reserve-Ratio	Yes	Yes	No	No	No	No	No
Idaho	Reserve-Ratio	No (a)	No	No	No	No	No	Yes
Illinois	Benefit-Ratio	No (a)	Yes	No	No	No	Yes	Yes
Indiana	Reserve-Ratio	Yes	Yes	No	No	No	No	No
Iowa	Benefit-Ratio	No (b)	No	No	No	No	Yes	Yes
Kansas	Reserve-Ratio	Yes	Yes	Yes	No	No	No	No
Kentucky	Reserve-Ratio	Yes	Yes	No	No	No	No	Yes
Louisiana	Reserve-Ratio	Yes	No	Yes	No	No	Yes	No
Maine	Reserve-Ratio	No (a)	No	No	No	No	Yes	No
Maryland	Benefit-Ratio	Yes	No	Yes	No	Yes	No	No
Massachusetts	Reserve-Ratio	No (b)	No	Yes	No	Yes	Yes	Yes
Michigan	Benefit-Ratio	No	Yes	Yes	No	No	No	No
Minnesota	Benefit-Ratio	Yes	Yes	No	No	No	No	Yes
Mississippi	Benefit-Ratio	Yes	Yes	Yes	No	No	No	No
Missouri	Reserve-Ratio	Yes	No	No	No	No	No	Yes
Montana	Reserve-Ratio	Yes	No	Yes	No	No	Yes	No
Nebraska	Reserve-Ratio	No (b)	No	Yes	No	No	Yes	Yes
Nevada	Reserve-Ratio	No (a)	Yes	No	No	No	Yes	Yes
New Hampshire	Reserve-Ratio	No (a)	Yes	No	Yes	Yes	Yes	Yes
New Jersey	Reserve-Ratio	Yes	No	Yes	No	No	No	Yes
New Mexico	Reserve-Ratio	Yes	No	Yes	No	No	Yes	Yes
New York	Reserve-Ratio	No (a)	Yes	Yes	No	No	Yes	No
North Carolina	Reserve-Ratio	Yes	No	Yes	No	No	Yes	No
North Dakota	Reserve-Ratio	Yes	No	Yes	No	No	Yes	Yes
Ohio	Reserve-Ratio	Yes	No	No	No	No	No	No
Oklahoma	State Experience	Yes	No	Yes	No	No	Yes	No
Oregon	Benefit-Ratio	Yes	No	No	No	No	Yes	No
Pennsylvania	Benefit-Ratio	Yes	No	Yes	No	No	Yes	No
Rhode Island	Reserve-Ratio	No (a)	No	Yes	No	No	Yes	Yes
South Carolina	Reserve-Ratio	No (a)	No	Yes	No	No	No	Yes
South Dakota	Reserve-Ratio	No (a)	No	Yes	No	No	Yes	Yes
Tennessee	Reserve-Ratio	Yes	No	Yes	No	No	Yes	No
Texas	Benefit-Ratio	Yes	No	Yes	No	No	Yes	Yes
Utah	Benefit-Ratio	Yes	No	No	No	No	Yes	No
Vermont	Benefit-Ratio	Yes	Yes	No	No	No	No	No
Virginia	Benefit-Ratio	No (a)	Yes	No	No	Yes	No	Yes
Washington	Benefit-Ratio	No (b)	No	Yes	No	No	Yes	No
West Virginia	Reserve-Ratio	Yes	No	Yes	No	No	Yes	Yes
Wisconsin	Reserve-Ratio	Yes	No	Yes	No	Yes	Yes	Yes
Wyoming	Benefit-Ratio	Yes	No	Yes	No	No	Yes	No
District of Columbia	Reserve-Ratio	Yes	Yes	Yes	No	No	Yes	No

(a) Benefits charged to most recent employer.
(b) Benefits charged to base-period employers, most recent first.
Source: U.S. Department of Labor

Table 20
Other State Unemployment Insurance Tax Base Criteria
As of January 1, 2009

State	Solvency Tax	Taxes for Socialized Costs or Negative Balance Employer	Loan and Interest Repayment Surtaxes	Reserve Taxes	Surtaxes for UI Administration or Non-UI Purposes	Temporary Disability Insurance	Voluntary Contributions	Time-Period to Qualify for Experience Rating (Years)
Alabama	No	Yes	Yes	No	Yes	No	No	1.0
Alaska	Yes	No	No	No	Yes	No	No	1.0
Arizona	No	No	No	No	Yes	No	Yes	1.0
Arkansas	No	No	Yes	No	Yes	No	Yes	3.0
California	No	No	No	No	Yes	Yes	Yes	1.0
Colorado	Yes	Yes	Yes	No	Yes	No	Yes	1.0
Connecticut	No	No	Yes	No	No	No	No	1.0
Delaware	Yes	No	Yes	No	Yes	No	No	2.0
Florida	No	No	No	No	No	No	No	2.5
Georgia	No	No	No	No	No	Yes	Yes	3.0
Hawaii	No	No	No	No	Yes	No	No	1.0
Idaho	No	No	Yes	Yes	Yes	No	No	1.0
Illinois	Yes	No	No	No	No	No	No	3.0
Indiana	No	No	No	No	Yes	No	Yes	3.0
Iowa	No	No	Yes	Yes	No	No	No	3.0
Kansas	No	No	No	No	Yes	No	Yes	2.0
Kentucky	No	No	No	No	No	No	Yes	3.0
Louisiana	Yes	Yes	Yes	No	Yes	No	Yes	3.0
Maine	No	No	Yes	No	Yes	No	Yes	2.0
Maryland	No	No	No	No	Yes	No	No	2.0
Massachusetts	No	No	Yes	No	Yes	No	Yes	1.0
Michigan	No	No	No	No	No	No	Yes	2.0
Minnesota	Yes	No	Yes	No	Yes	No	Yes	1.0
Mississippi	No	No	No	No	No	No	No	1.0
Missouri	No	No	Yes	No	Yes	No	Yes	1.0
Montana	No	No	No	No	Yes	No	No	3.0
Nebraska	Yes	No	No	Yes	No	No	Yes	1.0
Nevada	No	No	No	No	Yes	No	No	2.5
New Hampshire	Yes	No	No	No	No	No	No	1.0
New Jersey	Yes	No	Yes	No	Yes	Yes	Yes	3.0
New Mexico	No	No	No	Yes	Yes	No	Yes	3.0
New York	Yes	No	Yes	No	Yes	Yes	Yes	1.0
North Carolina	No	No	No	Yes	No	No	Yes	2.0
North Dakota	Yes	No	No	No	Yes	No	Yes	3.0
Ohio	No	Yes	No	No	No	No	Yes	1.0
Oklahoma	Yes	No	No	No	No	No	No	1.0
Oregon	No	No	Yes	No	No	No	No	1.0
Pennsylvania	Yes	No	Yes	No	No	No	Yes	1.5
Rhode Island	Yes	No	No	No	Yes	Yes	No	3.0
South Carolina	No	No	No	No	Yes	No	No	2.0
South Dakota	No	No	No	No	Yes	No	Yes	2.0
Tennessee	No	No	Yes	No	Yes	No	No	3.0
Texas	Yes	Yes	Yes	No	Yes	No	Yes	1.0
Utah	No	Yes	No	No	No	No	No	1.0
Vermont	No	No	No	No	No	No	No	1.0
Virginia	Yes	Yes	No	No	No	No	No	1.0
Washington	Yes	Yes	Yes	No	Yes	No	Yes	2.0
West Virginia	No	No	Yes	No	Yes	No	Yes	3.0
Wisconsin	No	Yes	Yes	No	ny	No	Yes	1.5
Wyoming	No	No	No	No	Yes	No	No	3.0
District of Columbia	No	No	No	No	No	No	No	3.0

Source: U.S. Department of Labor

Table 21
Property Tax Rates and Capital Stock Taxes
As of July 1, 2009

State	Property Tax Collections Per Capita	Property Tax Collections as a Percentage of Income	Capital Stock Tax Rate	Capital Stock Maximum Payment	Payment Options for CST and CIT
Alabama	$471	1.59%	0.180%	$15,000	Pay both
Alaska	$1,558	3.59%	None	n.a.	n.a.
Arizona	$945	2.93%	None	n.a.	n.a.
Arkansas	$520	1.86%	0.300%	Unlimited	Pay both
California	$1,153	2.72%	None	n.a.	n.a.
Colorado	$1,169	2.82%	None	n.a.	n.a.
Connecticut	$2,386	4.64%	0.310%	$1,000,000	Pay highest
Delaware	$681	1.23%	0.030%	$180,000	Pay both
Florida	$1,334	4.09%	None	n.a.	n.a.
Georgia	$1,038	3.08%	0.100%	$5,000	Pay Both
Hawaii	$915	2.34%	None	n.a.	n.a.
Idaho	$878	2.93%	None	n.a.	n.a.
Illinois	$1,684	4.16%	0.100%	$2,000,000	Pay both
Indiana	$995	3.03%	None	n.a.	n.a.
Iowa	$1,234	3.28%	None	n.a.	n.a.
Kansas	$1,297	3.62%	0.130%	$20,000	Pay both
Kentucky	$612	2.05%	None	n.a.	n.a.
Louisiana	$683	2.05%	0.300%	Unlimited	Pay both
Maine	$1,779	5.77%	None	n.a.	n.a.
Maryland	$1,164	2.95%	None	n.a.	n.a.
Massachusetts	$1,847	3.76%	0.260%	Unlimited	Pay both
Michigan	$1,474	4.59%	None	n.a.	n.a.
Minnesota	$1,171	2.80%	None	n.a.	n.a.
Mississippi	$800	3.24%	0.250%	Unlimited	Pay both
Missouri	$897	2.73%	0.030%	Unlimited	Pay both
Montana	$1,171	4.08%	None	n.a.	n.a.
Nebraska	$1,381	3.63%	0.030%	$15,000	Pay both
Nevada	$1,111	2.82%	None	n.a.	n.a.
New Hampshire	$2,304	5.96%	None	n.a.	n.a.
New Jersey	$2,634	5.82%	None	n.a.	n.a.
New Mexico	$529	1.69%	None	n.a.	n.a.
New York	$2,096	4.11%	0.150%	$10,000,000	Pay highest
North Carolina	$827	2.30%	0.150%	$75,000	Pay both
North Dakota	$1,080	2.72%	None	n.a.	n.a.
Ohio	$1,335	4.00%	0.160%	$60,000	Pay highest
Oklahoma	$555	1.86%	0.130%	$20,000	Pay both
Oregon	$1,042	2.61%	None	n.a.	n.a.
Pennsylvania	$1,251	3.46%	0.290%	Unlimited	Pay both
Rhode Island	$1,949	5.36%	0.030%	Unlimited	Pay highest
South Carolina	$1,019	3.60%	0.100%	Unlimited	Pay both
South Dakota	$1,042	2.69%	None	n.a.	n.a.
Tennessee	$719	2.11%	0.250%	Unlimited	Pay both
Texas	$1,393	3.59%	None	n.a.	n.a.
Utah	$762	2.34%	None	n.a.	n.a.
Vermont	$2,050	5.80%	None	n.a.	n.a.
Virginia	$1,357	3.23%	None	n.a.	n.a.
Washington	$1,147	2.79%	None	n.a.	n.a.
West Virginia	$622	2.41%	0.550%	Unlimited	Pay both
Wisconsin	$1,513	4.27%	None	n.a.	n.a.
Wyoming	$2,118	5.06%	0.020%	Unlimited	Pay both
District of Columbia	$2,187	1.70%	None	n.a.	n.a.

Source: Census Bureau, CCH, Tax Foundation.

Table 22
Other Property Tax Base Criteria
As of July 1, 2009

State	Intangible Property	Inventory	Real Estate Transfer	Estate Tax	Inheritance Tax	Generation-Skipping Transfer Tax	Gift Tax
Alabama	Yes	No	Yes	Copies Federal System	No	No	No
Alaska	No	Yes	No	Copies Federal System	No	No	No
Arizona	No	No	No	Copies Federal System	No	No	No
Arkansas	No	Yes	Yes	Copies Federal System	No	No	No
California	No	No	Yes (a)	Copies Federal System	No	No	No
Colorado	No	No	No (b)	Copies Federal System	No	No	No
Connecticut	No	No	Yes	Decoupled	No	No	Yes
Delaware	No	No	Yes	Copies Federal System	No	No	No
Florida	No	No	Yes	Copies Federal System	No	No	No
Georgia	Yes	Yes	Yes	Copies Federal System	No	No	No
Hawaii	No	No	Yes	Copies Federal System	No	No	No
Idaho	No	No	No	Copies Federal System	No	No	No
Illinois	No	No	Yes	Decoupled	No	No	No
Indiana	No	No	No	Copies Federal System	Yes	No	No
Iowa	Yes	No	Yes	Copies Federal System	Yes	No	No
Kansas	No	No	Yes	Decoupled	No	No	No
Kentucky	No	Yes	Yes	Copies Federal System	Yes	No	No
Louisiana	Yes	Yes	No	Copies Federal System	No	No	No
Maine	No	No	Yes	Decoupled	No	No	No
Maryland	No	Yes	Yes	Decoupled	Yes	No	No
Massachusetts	No	Partial	Yes	Decoupled	No	No	No
Michigan	No	No	Yes	Copies Federal System	No	No	No
Minnesota	No	No	Yes	Copies Federal System	No	No	No
Mississippi	Yes	Yes	No	Copies Federal System	No	No	No
Missouri	No	No	No	Copies Federal System	No	No	No
Montana	No	No	No	Copies Federal System	No	No	No
Nebraska	No	No	Yes	Decoupled	Yes	No	No
Nevada	No	No	Yes	Copies Federal System	No	No	No
New Hampshire	No	No	Yes	Copies Federal System	No	No	No
New Jersey	No	No	Yes	Decoupled	Yes	No	No
New Mexico	No	No	No	Copies Federal System	No	No	No
New York	No	No	Yes	Decoupled	No	No	No
North Carolina	Yes	No	Yes	Decoupled	No	No	Yes
North Dakota	No	No	No	Copies Federal System	No	No	No
Ohio	Yes	No	Yes	Decoupled	No	No	No
Oklahoma	No	Yes	Yes	Decoupled	No	No	No
Oregon	No	No	No	Decoupled	No	No	No
Pennsylvania	Yes	No	Yes	Decoupled	Yes	No	No
Rhode Island	No	No	Yes	Decoupled	No	No	No
South Carolina	No	No	Yes	Copies Federal System	No	No	No
South Dakota	No	No	Yes	Copies Federal System	No	No	No
Tennessee	Yes	No	Yes	Copies Federal System	Yes	No	Yes
Texas	Yes	Yes	No	Copies Federal System	No	No	No
Utah	No	No	No	Copies Federal System	No	No	No
Vermont	No	Yes	Yes	Copies Federal System	No	No	No
Virginia	No	Yes	Yes	Copies Federal System	No	No	No
Washington	No	No	Yes	Decoupled	No	No	No
West Virginia	No	Yes	Yes	Copies Federal System	No	No	No
Wisconsin	No	No	Yes	Copies Federal System	No	No	No
Wyoming	No	No	No	Copies Federal System	No	No	No
District of Columbia	No	No	Yes	Decoupled	No	No	No

(a) No statewide real estate transfer tax, but every county has one.
(b) De minimis tax of 0.01 percent of property value.
Sources: Commerce Clearing House, Tax Foundation.

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