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# PAYCHECK\$ and POLITICS

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## Twenty Progressive Ways to Fund Education Reform This is Not Your David Letterman Top Ten List!

According to a recent study by the Joint Committee on Educational Adequacy, it will cost \$847 million to reform the Arkansas education system and provide an adequate education for the state's children (not counting the cost of new school facilities). While it's anybody's guess as to how much new tax revenue the legislature will be willing to raise during the December special session on education, most agree that the state needs to make a good faith effort to raise a large portion of the revenue needed to show compliance with the Arkansas Supreme Court mandate in the Lake View case.

During the 2003 regular session earlier in the year, a broad range of bills were introduced as possible ways to raise new education dollars, including measures that would increase the revenue from personal and corporate income taxes, sales taxes, severance taxes, and property taxes.

Many of these ideas are likely to be considered again when the Arkansas General Assembly meets in its December special session on education reform and financing. Obviously, not all of these options are created equal. They raise different amounts of revenue and affect Arkansas families at different income levels in different ways.

Before reviewing these options, it's helpful to define what is meant by a "fair" tax system. Historically, a "progressive" tax system has been regarded as the fairest type of tax system. Under a "progressive" tax system, the percent of the income you pay in taxes increases as your income increases. A progressive tax system is based on the idea that those with a greater ability to pay contribute a larger share of their income in taxes. In contrast, a regressive system is generally regarded as the least fair. Under a regressive

system, low-income families pay a greater percent of their income in taxes than do upper-income families.

Currently the Arkansas tax system is very regressive. As a percent of their income, low- and middle-income families pay more in state and local taxes than the state's richest families. Low-income families pay 11.3 percent of their annual income in state and local taxes, middle income families pay 10.7 percent, while the top one percent pay only 5.8 percent.

Some proposals, such as increasing the state sales tax rate would place a disproportionate burden on low- and middle-income families and make the tax system more regressive. Others, such as increases in personal and corporate income taxes, would place a higher burden on those with higher incomes and a greater ability to pay and make the tax system more fair and progressive. This issue brief lists 20 progressive ways (or at least more progressive than simply raising the sales tax rate) to pay for education reform and minimize the burden of any tax increases on low- and middle-income families.

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# 20 Progressive Ways to Fund Education

## Corporate Income Taxes

1. New top corporate income tax of 7.0% (top rate is currently 6.5% on a company's net income over \$100K).<sup>b</sup> ----- \$15M
2. 1% Corporate income tax surcharge - \$1.5 million for each 1%.<sup>a</sup> ----- \$1.5M
3. Flat corporate income tax of 6.5% on all of the net income of all corporations.<sup>a</sup> ----- \$6.7M
4. Flat corporate income tax of 6.5% on all of the net income for corporations w/earnings over 100K.<sup>a</sup> ----- \$2.3M
5. Change the severance tax to 5% of market value.<sup>b</sup> ----- \$35M
6. Close corporate income tax loopholes (domestic tax sheltering loopholes only).<sup>c</sup> ----- \$44M
13. Alternative minimum tax on the personal income tax (7% of federal base).<sup>b</sup> ----- \$8M
14. Repeal capital gains tax exclusion (eliminates 30% cap gains exclusion).<sup>b</sup> ----- \$34M
15. Decouple from the federal repeal of the estate tax.<sup>b</sup> (because of federal changes, the Arkansas estate tax will disappear in coming years) ----- \$20M
16. Conform to the feds on state personal income tax treatment of pensions.<sup>b</sup> (Arkansas currently gives more preferable treatment to this income than do the feds). ----- \$39M
17. Conform to the feds on state personal income tax treatment of social security.<sup>b</sup> (Arkansas currently gives more preferable treatment to this income than do the feds). ----- \$39M

## Personal Income Taxes

7. New top bracket on personal income tax of 8% for Income over \$100K<sup>b</sup> (top rate is currently 7% for income over \$27K) ----- \$34M
8. New top bracket on personal income tax of 8% for income over \$200K.<sup>b</sup> ----- \$20M
9. New top bracket on personal income tax of 9% for income over \$200K.<sup>b</sup> ----- \$40M
10. New top brackets on personal income tax of 8% over \$100K and 9% over \$200K.<sup>b</sup> ----- \$54M
11. Across the board tax increase of 1% on personal income tax (e.g., each bracket would increase by 1%, e.g., bottom bracket of 1% would rise to 2%, 7% to 8%).<sup>b</sup> ----- \$344M
12. Increase all personal income tax rates by 10% (e.g., bottom bracket of 1.0% would increase to 1.1%, 2.5% to 2.75, etc.).<sup>b</sup> ----- \$164M
18. Conform to the feds on state personal income tax treatment of both pensions and social security income.<sup>b</sup> (Arkansas currently gives more preferable treatment to this income than do the feds). ----- \$85M

## Property Taxes

19. Target the \$300 property tax credit to families with incomes less than \$30K (currently all homeowners, regardless of income level, are eligible for the credit).<sup>b</sup> ----- \$100M

## Sales Taxes

20. Remove sales tax exemptions for goods (\$582M) and levy sales tax on non-medical services (\$179M) ----- \$761M

### Notes:

- a. Estimate by the Arkansas Department of Finance and Administration.
- b. Estimate by the Institute on Taxation and Economic Policy
- c. Estimate by the Multi-State Tax Commission.