



## TESTIMONY: PENNSYLVANIA FISCAL AND ECONOMIC OUTLOOK PANEL AT YORK COLLEGE

### Introduction

Good morning/afternoon, and thank you so much for having me. As mentioned, my name is Ashley Klingensmith, and I am the Pennsylvania State Director for Americans for Prosperity. For those unfamiliar, Americans for Prosperity is a non-profit, non-partisan grassroots advocacy organization that engages in many of the important policy questions we face today. Our perspective on these issues is always one of removing the barriers that prevent individuals from earning their own success, contributing to their communities, and living a life full of dignity and personal fulfillment.

So, it should come as no surprise that when I was asked to speak regarding our state's economic growth, the first question that came to my mind was: how do our current policies affect Pennsylvanians' ability to build their own success and act as an engine of growth for our state as a whole?

The answer comes down to a few primary categories of policy that I'll be diving into a little more today. But before I dig in, I want to start with a caveat. Our state economy is massive and endlessly complex – it's beyond any one of us to direct it to achieve optimal growth. But, what we can do is create the conditions – the environment – for success, and trust that Pennsylvanians will take hold of these opportunities to do something truly special that will benefit us all.

That being said, there are three things that have an outsized effect on economic growth in any state: the tax climate, the regulatory environment, and employment policies.

### Tax Climate

Pennsylvania currently has the 34<sup>th</sup> best business tax climate in the country, according to the Tax Foundation.<sup>1</sup> While this is by far not the worst, it is below average and I think we can do better. Among the taxes affecting business and economic growth is the corporate income tax. In Pennsylvania our corporate income tax is 4.24 percent, making our rate the eighth highest in the country. Why does this matter? Research has found that corporate tax rates have a strong effect on business formation in a state. When a state cuts its corporate income tax by a percentage point, it sees a three to four percent increase in the number of business establishments.<sup>2</sup> Corporate tax increases are similarly associated with slower economic growth.

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<sup>1</sup> Jared Walczak, "2019 State Business Tax Climate Index," The Tax Foundation, <https://taxfoundation.org/publications/state-business-tax-climate-index/>, (September 2018)

<sup>2</sup> Juan Carlos Suárez Serrato and Owen Zidar, "Who Benefits from State Corporate Tax Cuts? A Local Labor Markets Approach with Heterogeneous Firms," *National Bureau of Economic Research*, <https://www.nber.org/papers/w20289.pdf>, (July, 2014)

Beyond just rates, we should be looking at the structure of our tax system. A massive amount of capital is tied up in compliance costs for an overly complex tax structure. Such complexity creates unnecessary economic inefficiencies that have nothing to do with task of collecting revenues to fund the essential services we need and expect from our government. It is estimated that the federal Tax Cuts and Jobs Act, by simplifying the tax code, could result in compliance savings ranging from \$3.1 billion to \$5.4 billion nationwide.<sup>3</sup> Pennsylvania can and should mirror these streamlining efforts in our own tax code. Not only will reductions in rates free up capital for further investment, but compliance savings can similarly be used to expand businesses, create new jobs, and raise wages in an increasingly competitive labor market.

There's also another element to streamlining our tax code that will reap major benefits for economic growth: the elimination of targeted deductions and tax credits to favored businesses. Targeted economic development incentives, often referred to as corporate welfare, distort markets and have failed to yield long-term economic growth time and time again. As the recent Amazon HQ2 battle demonstrated, it is only too easy to convince well-meaning lawmakers to mortgage their state's finances in the pursuit of "economic development." And the irony is that these incentives are not even a primary factor for most businesses when deciding where to locate. Factors such as the presence of a skilled workforce, cost of living, infrastructure, and an accessible consumer marketplace are all more important to businesses. It is estimated that at least 75 percent of firms that receive some form of tax incentive would have made a similar decision regarding their facility location(s) and personnel without the incentive.<sup>4</sup>

With the money our state spends on special tax treatment for a favored few, we could reduce overall tax rates and address many of these more important factors to economic growth. The average known state subsidy bid for Amazon HQ2 was \$6.75 billion. For that amount, Pennsylvania could reduce its corporate income tax rate by 10.78 percent, fund nearly 17,000 four-year college scholarships for Pennsylvania students, or fully fund our statewide road maintenance for four years.<sup>5</sup> To me, any of these options would yield greater long-term growth and a more dynamic economy than offering the funding to one private corporation on a silver platter. In fact, if Pennsylvania eliminated all of the favorable tax incentives it already supplies, we could reduce our corporate income tax rate by 6.1 percent!<sup>6</sup>

## Regulatory Environment

I'm going to turn my attention now from tax policy to another policy consideration that can be incredibly costly for economic growth in our state, and that is regulation. A disproportionate regulatory burden, one that reaches beyond basic public health and safety concerns, presents a barrier to entry into the marketplace that many would-be entrepreneurs and job creators simply cannot overcome. In fact, a 10 percent increase in

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<sup>3</sup> Erica York, "Reviewing Different Methods of Calculating Tax Compliance Costs," The Tax Foundation, <https://taxfoundation.org/different-methods-calculating-tax-compliance-costs/>, (August, 2018)

<sup>4</sup> Timothy J. Bartik, "'But for' Percentages for Economic Development Incentives: What Percentage Estimates Are Plausible Based on the Research Literature?" Upjohn Institute Working Paper, W.E. Upjohn Institute, Kalamazoo, Michigan, (July, 2018)

<sup>5</sup> Michael Farren and Anne Philpot, "With Amazon HQ2, the Losers Are the Winners: Why Economic Development Subsidies Hurt More than They Help," Mercatus Center, George Mason University, Arlington, Virginia, [https://www.mercatus.org/system/files/farren\\_and\\_philpot\\_-\\_policy\\_brief\\_-\\_amazon\\_hq2\\_the\\_story\\_so\\_far\\_-\\_v1.pdf](https://www.mercatus.org/system/files/farren_and_philpot_-_policy_brief_-_amazon_hq2_the_story_so_far_-_v1.pdf), (November, 2018)

<sup>6</sup> Matthew D. Mitchell and Tamara Winter, "The Opportunity Cost of Corporate Welfare," Mercatus Center, George Mason University, Arlington, Virginia, <https://www.mercatus.org/publications/corporate-welfare/opportunity-cost-corporate-welfare>, (May, 2018)

the intensity of regulation leads to a statistically significant decrease in the number of new businesses getting started, as well as a significant decrease in hiring among all firms – old and new, small and large.<sup>7</sup> With so many jobs on the line, it is imperative that we get the balance right when it comes to regulatory policy.

Yet the *Pennsylvania Code* is prohibitively large and difficult to fully understand. The code contains 153,661 restrictions, 12.8 million words, and would take 18 weeks to read through if a person read 300 words per minute for 40 hours per week.<sup>8</sup> It's a lot to ask of anyone to know when they are, or are not, in compliance with such a large document. And that doesn't even include federal and local regulations.

This is why we need a bipartisan, evidence-based approach to crafting and managing regulations – as well as sunseting obsolete regulations. Models have begun to pop up around the country for such reforms. Most involve a powerful combination of the following activities: 1.) Counting the number, size, and severity of all state regulations, 2.) Capping the cumulative size of the state regulatory burden, 3.) Working with the rule-making agencies themselves to understand which regulations are duplicative or obsolete and can therefore be cut, and which regulations need to be updated or streamlined to make compliance easier, and/or 4.) Establishing an analysis unit to evaluate the potential economic impacts of various regulations and responsibly weigh them against the potential benefits to public health and safety.

Similar bipartisan legislation has already been introduced here in Pennsylvania. House Bill 995 has 24 sponsors (14 Democrats and 10 Republicans) and would establish a pilot program within certain agencies requiring them to count their regulations and compliance costs, cap them, and propose cuts equal to 25 percent of their total regulatory burden.<sup>9</sup> This type of innovation could truly unleash the economic potential of small businesses in our state – many of whom are disproportionately affected by regulatory compliance burdens.

### Employment Policy

As I move into our final category, employment policy, there is a very important issue that straddles both employment policy and the regulatory barriers we just discussed – and that issue is occupational licensing. If you are not familiar with this particular type of regulation, it is essentially a requirement that someone obtain permission directly from the state government before practicing in a certain field. Unlike other types of regulation (like registration, inspections, and sanctions), which provide a structure for monitoring the quality of a good or service and providing consequences if a professional jeopardizes the health and safety of another, occupational licensure does not allow a person to practice their trade at all until they meet the state's often onerous requirements to obtain a license.

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<sup>7</sup> James Bailey and Diana Thomas, "Regulating Away Competition: The Effect of Regulation on Entrepreneurship and Employment," Mercatus Center, George Mason University, Arlington, Virginia, <https://www.mercatus.org/publication/regulating-away-competition-effect-regulation-entrepreneurship-and-employment>, (September, 2015)

<sup>8</sup> James Broughel, Oliver Sherouse, and Daniel Francis, "A Snapshot of Pennsylvania Regulation in 2017," Mercatus Center, George Mason University, Arlington, Virginia, <https://www.mercatus.org/system/files/broughel-snapshot-pennsylvania-regulation-2017-brief-v1.pdf>, (April, 2017)

<sup>9</sup> PA 2019 HB 995, <https://www.legis.state.pa.us/cfdocs/billinfo/billinfo.cfm?year=2019&sind=0&body=H&type=B&bn=995>

There is a large body of research detailing how ineffective occupational licensure is as a means to protect public health and safety – and even to ensure quality. Perhaps one of the best recent examples of this is an excellent report put out by the Obama administration – their review of the existing literature on this subject found that, “Stricter licensing was associated with quality improvements in only 2 out of the 12 studies reviewed. There is also evidence that many licensing boards are not diligent in monitoring licensed practitioners, which contributes to a lack of quality improvement under licensing. These boards often rely on consumer complaints and third-party reports to monitor practitioner quality, but only a small fraction of consumer complaints result in any kind of disciplinary action.”<sup>10</sup> If this regulatory framework is not efficient at enforcing quality standards, why allow it to get in the way of individuals trying to make a living?

When it comes to occupational licensing, Pennsylvania is considered to have less onerous regulations than many other states, but this is not a good way to judge our state because even the best states relative to others are in need of significant reform to increase employment opportunities and consumer access. There are also a number of low to moderate income occupations Pennsylvania licenses that many other states do not – including upholsterers, weighers, taxidermists, and auctioneers. For that last one, we require 140 days of education time to get licensed – while in the meantime we have highly competent EMTs who serve the public with only 35 days of education time required to get licensed.<sup>11</sup> It seems that even in Pennsylvania we still have some work to do on the occupational licensing front.

In fact, with almost 20% of our workforce requiring permission from government to work, one study estimates that each year licensing costs us over 89,000 jobs, \$368 million in deadweight economic losses, and over \$9.4 billion in misallocated economic resources, which represents people spending money where they would not have if only Pennsylvania’s licensing laws weren’t creating harmful barriers to access.<sup>12</sup>

Finally, I’d like to take a little time talking about public sector workers, and their contributions to our state economy. In fiscal year 2014, the state employed 161,369 employees, with localities employing an additional 400,000 or so. State employee payroll accounted for nearly \$800 million per month. With state and local employee payroll taken together, it was over \$2.6 billion per month.<sup>13</sup>

Ideally, these public employees should have full command of their salaries – those dollars should be theirs to save, invest, or spend as they see fit – providing valuable investment dollars and economic activity. Yet many workers do not fully understand their rights to their own salaries as outlined in the landmark *Janus v. AFSCME* Supreme Court ruling passed down just a year ago. Based on this ruling, all public employees have certain rights – we call them *Janus* Rights. Chief among them is that they cannot be compelled to have public sector union dues deducted from their paychecks as a condition of their employment. While this ruling was certainly a contentious one, the good news for our state’s economy is that these dollars are now free for

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<sup>10</sup> Department of the Treasury Office of Economics Policy, the Council of Economic Advisors, the Department of Labor, “Occupational Licensing: A Framework for Policymakers,” [https://obamawhitehouse.archives.gov/sites/default/files/docs/licensing\\_report\\_final\\_nonembargo.pdf](https://obamawhitehouse.archives.gov/sites/default/files/docs/licensing_report_final_nonembargo.pdf), (July, 2015)

<sup>11</sup> Dick M. Carpenter II, Lisa Knepper, Kyle Sweetland, and Jennifer McDonald, “License to Work, 2<sup>nd</sup> Edition,” The Institute for Justice, <https://ij.org/report/license-work-2/tw-state-profiles/tw2-pennsylvania/>, (November, 2017)

<sup>12</sup> Institute for Justice, “At What Cost,” <https://ij.org/report/at-what-cost> (November, 2018)

<sup>13</sup> Governing Magazine, “States with Most Government Employees: Totals and per Capita Rates,” <https://www.governing.com/gov-data/public-workforce-salaries/states-most-government-workers-public-employees-by-job-type.html>, (March, 2014)

public employees to direct how they wish – whether that be union activity or not. Simply by having the choice of how to spend this additional portion of their salaries, market forces work better and we all benefit. The now voluntary nature of union membership for our public servants helps ensure that the relationship between workers, government unions, and government as employer are more mutually beneficial. That’s one reason we’ve been supporting House Bill 785, which notifies workers of their rights under the *Janus* ruling – rights they were never entitled to for decades in our state that many still do not fully realize. It is the duty of our government to honor the U.S. Constitution and ensure our public workers are able to exercise their First Amendment rights.<sup>14</sup>

### Conclusion

Since my time is now winding down, I’d just like to conclude with a few thoughts.

I hope everyone comes away from this with a message of optimism – there’s a lot of things that are going well and many more that are within our reach to improve. But as we continue the discussion regarding the best ways to grow our economy, if nothing else I would encourage all of us as a community of policymakers and advocates to focus on solutions that are accessible to **all** Pennsylvanians, not just those who have particular connections or work in a certain favored industry. None of us know what the future holds, and there are likely a lot of great employment and investment opportunities on the horizon. Rather than trying to anticipate what those opportunities will be, we can prepare our policy landscape such that every Pennsylvanian will be able to take advantage of those opportunities when they arise.

Thank you again to the organizers for the invitation to participate, and thanks to you all for being so engaged during my comments. I will be happy to answer questions during our Q&A portion.

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<sup>14</sup> PA 2019 HB 785, <https://www.legis.state.pa.us/cfdocs/billinfo/billinfo.cfm?year=2019&ind=0&body=H&type=B&bn=785>

## #34 PENNSYLVANIA

Pennsylvania		
	Rank	Score
Overall Rank	34 (+0)	4.85
Corporate Taxes	43 (+0)	4.24
Individual Taxes	18 (+0)	5.41
Sales Taxes	21 (+0)	4.97
Property Taxes	34 (+0)	4.77
Unemp. Insur. Taxes	46 (+0)	4.14

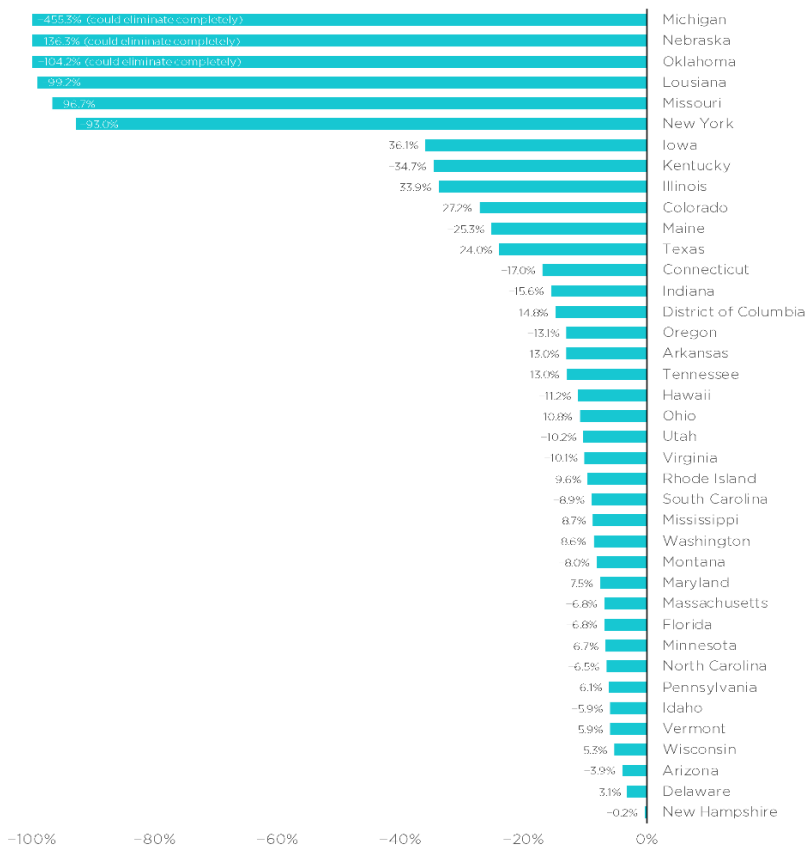
Neighboring States	Top States	Bottom States
#11 Delaware #19 West Virginia #34 Pennsylvania #40 Maryland #42 Ohio #48 New York #50 New Jersey	#1 Wyoming #2 Alaska #3 South Dakota #4 Florida #5 Montana	#50 New Jersey #49 California #48 New York #47 Connecticut #46 District of Columbia

TABLE 1. TRADEOFFS IN STATE-PROVIDED PUBLIC SERVICES AND TAX CUTS THAT COULD BE FUNDED INSTEAD OF THE AMAZON HQ2 SUBSIDY

Jurisdiction	Amount that corporate income taxes rates could be reduced (percent)	Number of full-tuition scholarships that could be funded each year at the state's flagship public university	Number of years of state-wide road maintenance that could be funded
California	3.62%	22,206	4
Colorado	84.04%	28,732	14
District of Columbia	17.64%	13,026	40
Florida	17.90%	46,151	5
Georgia	34.79%	24,915	14
Illinois	23.89%	24,464	6
Indiana	57.32%	27,952	8
Maryland	70.23%	62,598	14
Massachusetts	13.73%	38,215	17
New Jersey	15.22%	11,825	6
New York	5.42%	44,145	3
North Carolina	71.94%	41,950	6
Ohio	11.87%	27,801	10
Pennsylvania	10.78%	16,907	4
Tennessee	4.30%	22,702	15
Texas	5.66%	28,274	2
Virginia	45.16%	22,059	4

Notes: For most states we use \$6.75 billion over 15 years as the expected Amazon HQ2 state subsidy, which is based on the average of publicly available state-level subsidy bids. For New Jersey and Maryland, we use the actual state legislature-approved subsidy bid: \$5 billion over 20 years and \$8.5 billion over 10 years, respectively.  
Source: See appendix for data sources and calculation methodology.

### Potential Reduction in Corporate Income Taxes by State



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Notes: South Dakota and Wyoming have no corporate income tax. Nevada, Ohio, Texas, and Washington have a gross receipts tax instead of a corporate income tax. Ohio, Texas, and Washington calculations are based on that tax base, while Nevada's gross receipts revenue data are not available, so they are omitted from this calculation. See footnote for a breakdown of cost savings.  
Source: Authors' calculations based on data from Good Jobs First, "State Tax Revenue Lost to 'No Abolishment Programs,'" accessed April 30, 2018, <https://www.goodjobsfirst.org/files/site/ckan/78/0285>; National Association of State Budget Officers, *State Expenditure Report 2017*, 33. Produced by Matthew D. Mitchell and Tamara Winsor, May 2018.