



# CIVITAS

2018 Legislative Agenda

# BUDGET & TAXES



## **Budget & Tax Issues**

In 2013, North Carolina passed historic tax reforms, providing arguably the largest tax cuts in the state's history. Legislators rightly recognized that allowing hard-working taxpayers to keep more of what they earn is not only the moral thing to do, but found such policies stimulate economic growth as well.

Since passage of the tax reforms, conservative lawmakers have held state spending growth in check. Annual growth rates have consistently remained below the combination of population growth plus inflation, levels recommended by [Taxpayer Bill of Rights](#) proposals.

The combination of reform and spending restraint has produced impressive results. Following the reforms, the Tax Foundation boosted North Carolina's ranking in their business tax climate index from an abysmal 44<sup>th</sup> to 15<sup>th</sup>, the biggest improvement in one year of any state. Additional tax cuts in subsequent years have helped boost NC's ranking to 11<sup>th</sup> this year.

North Carolina's annual average economic growth rate of 2.5 percent since the beginning of 2013 is 13<sup>th</sup> best in the nation and above both national and regional averages. Our state's job growth rate of 11 percent during that time likewise exceeds national and regional averages. It has also helped to produce more than 440,000 net new jobs. Moreover, not only did reforms help to cut in half North Carolina's traditional unemployment rate, but North Carolina's "U-6 rate" - which measures joblessness, people dropping out of the workforce and the underemployed - also enjoyed the sixth-best improvement rate in the country, an improvement rate higher than any other Southeastern state.<sup>i</sup>

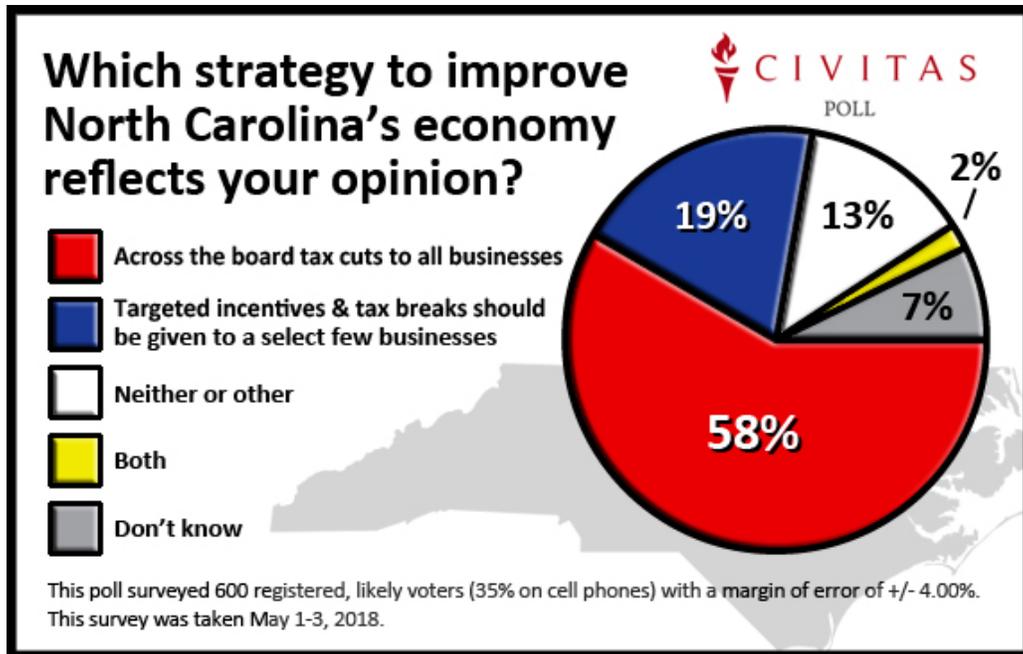
Furthermore, in recent years the combination of tax cuts and tight budgets have generated annual budget surpluses of hundreds of millions of dollars, helping legislators to build up a Rainy-Day Fund of \$1.8 billion - an all-time high.

Despite the progress, however, North Carolina still has plenty of room for improvement. State legislators continue to be enamored with corporate welfare schemes. One recent report pointed out that the state has [doled out more than \\$1 billion in "economic incentives"](#) in the last five years alone. After the film tax credit expired in 2014, legislators have been rapidly expanding a newly-created film production grant.

Civitas opposes such policies. Cronyism rewards the politically-favored corporations and industries at the expense of all other businesses. Corporate incentives also work to sharpen the urban-rural economic divide in the state, as most incentives tend to be awarded to companies in large urban areas. As a result, other businesses are left to pay higher taxes than they would otherwise. Civitas believes that if the state taxes businesses, the rules should be the same for all.

North Carolina citizens agree on this point. When asked in a statewide May 2018 Civitas poll "Which strategy to improve the state's economy best reflects your opinion", 58 percent replied "across the board

tax cuts for all businesses” compared to just 19 percent that responded with “targeted incentives and tax breaks given to a few select businesses.”



To foster a more competitive climate for jobs and economic growth, North Carolina needs to remove government barriers and disincentives which hamper productive economic activity. Burdensome regulations, occupational licensing, high taxes, cronyism and growing government spending threaten the progress we've already made and cloud North Carolina's economic outlook.

The Civitas Institute believes that the best thing state government can do for North Carolina's economy is not only to get out of the way but to also create a climate that encourages entrepreneurship and allows more economic activity outside the scope of government control. A significant majority of North Carolinians share this sentiment. In a May 2017 Civitas Poll, virtually twice as many respondents said that “cutting state taxes to boost the economy” (47%) would most benefit their personal situation than replied “increasing state spending to boost the economy” (24%).

The following key – and popular – recommendations can help North Carolina to not only continue the positive economic momentum of recent years, but to also become one of the nation's strongest states for job creation and economic growth:

- *Eliminate the corporate income tax* – Of the 44 states that levy a corporate income tax, North Carolina's 3 percent rate is the lowest. It is scheduled to fall to 2.5 percent next year. Research shows that the corporate tax is both most harmful to economic growth and the most volatile source among the major sources of state tax revenue. At such a low rate, it would be best to

eliminate this tax completely. It makes little sense to continue imposing such a destructive and unreliable tax.

- *Stop corporate welfare and level the playing field for all businesses* – Productive resources should be in the hands of entrepreneurs and businesses that most efficiently satisfy consumer needs and wants. Business success shouldn't be determined by which companies have highly-paid lobbyists. Moreover, government handouts and targeted tax credits distort the state's economy and lead to an environment ripe for corruption. Eliminating crony programs like corporate incentives will enable North Carolina to provide far more effective across-the-board tax relief, including elimination of the state corporate income tax.
- *Reduce the cap on the state's income tax* – The North Carolina State Constitution currently limits the state income tax to 10 percent of income. Legislation that would ask voters to approve a constitutional amendment to lower that cap to 5.5 percent ([SB 75](#)) passed the Senate in 2017 but failed to pass the House. While recent conservative leadership has done an excellent job of reducing taxes and keeping them low, a constitutional amendment is the best way to protect North Carolina taxpayers from big tax hikes by future legislatures. A February 2018 Civitas poll found overwhelming support for an amendment, with 68 percent of respondents supporting the amendment, while only 21 percent opposed.
- *Formalize spending restraint measures* – Similar to capping the income tax rate to prevent future legislative tax hikes, adoption of a Taxpayer Bill of Rights amendment to the North Carolina State Constitution would safeguard future state budgets from out-of-control spending. Such an amendment would limit annual spending growth to a rate tied to the combination of inflation plus population growth. Doing so would rein in and smooth out budget spending trends. While the amendment's ultimate goal is to actually reduce the state budget, ensuring growth rates stay under sensible levels is a crucial step toward ensuring fiscal responsibility. Support for a Taxpayer Bill of Rights amendment garners significant support among voters as well, with 57 percent of respondents supporting the measure compared to only 17 percent in opposition, according to an April 2016 Civitas poll.

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<sup>i</sup> Source: John Hood. "Nearby Successes Don't Disprove Conservatism", Carolina Journal online, March 5, 2018. Available online at: <https://www.carolinajournal.com/opinion-article/nearby-successes-dont-disprove-conservatism/>