



## **A Balanced Approach Promoted Ohio Recovery after Previous Recessions**

By Jon Honeck, Ph.D.  
Director of Public Policy and Advocacy  
October 29, 2009

The historical record shows that raising taxes during a recession will not harm an economic recovery. In fact, just the opposite is likely to occur. Ohio raised taxes in the recessions of the 1980s and 1990s to fund vital public services, and job growth was strong during the economic recoveries that followed. In the current decade, the state saw moderate job growth under a temporary sales tax and then lost jobs starting in 2006 *after* taxes were cut.

In fact, economic trends suggest that Ohio should cancel – rather than just postpone – the final income tax cut and respond to the current crisis with a balanced approach that includes new revenues. Current policies rely too much on spending cuts that harm Ohio families and will have long-lasting negative effects. While Governor Ted Strickland’s proposal, passed by the House, is a step in the right direction, more needs to be done to make sure Ohio provides vital services at a time when demand for them is increasing.

The crushing national recession has brought record declines in tax revenue to states around the country. A problem of this magnitude can’t be solved by any one strategy. Most states have cut spending but they also have made use of federal stimulus funds, tapped reserves, and raised revenues. State revenues recover only slowly after recessions, so the fiscal crunch from a severe recession is likely to continue for years.<sup>1</sup>

For Ohio to do the same now would be in keeping with the state’s bipartisan tradition. Each of the past five elected governors presided over revenue increases in response to a recession, generally after making a number of spending cuts.<sup>2</sup> A revenue crisis in the early 1970s led Governor John Gilligan, a Democrat, to convince the legislature to adopt Ohio’s personal income tax and an income tax component to the corporate franchise tax.<sup>3</sup> In a deep recession in the early 1980s, the legislature increased revenues by adding new temporary tax brackets on high-income earners under Governor Jim Rhodes, a Republican, and then made the brackets permanent with higher rates under Governor Richard Celeste, a Democrat. Following a prolonged decline in state revenues after the recession of the early 1990s, the legislature once again turned to tax increases to balance the budget under Governor George Voinovich, a Republican. Earlier in this decade, the state used a temporary sales tax increase under Governor Bob Taft, a Republican, to get through a downturn.

### **1980s: New Brackets, Strong Recovery**

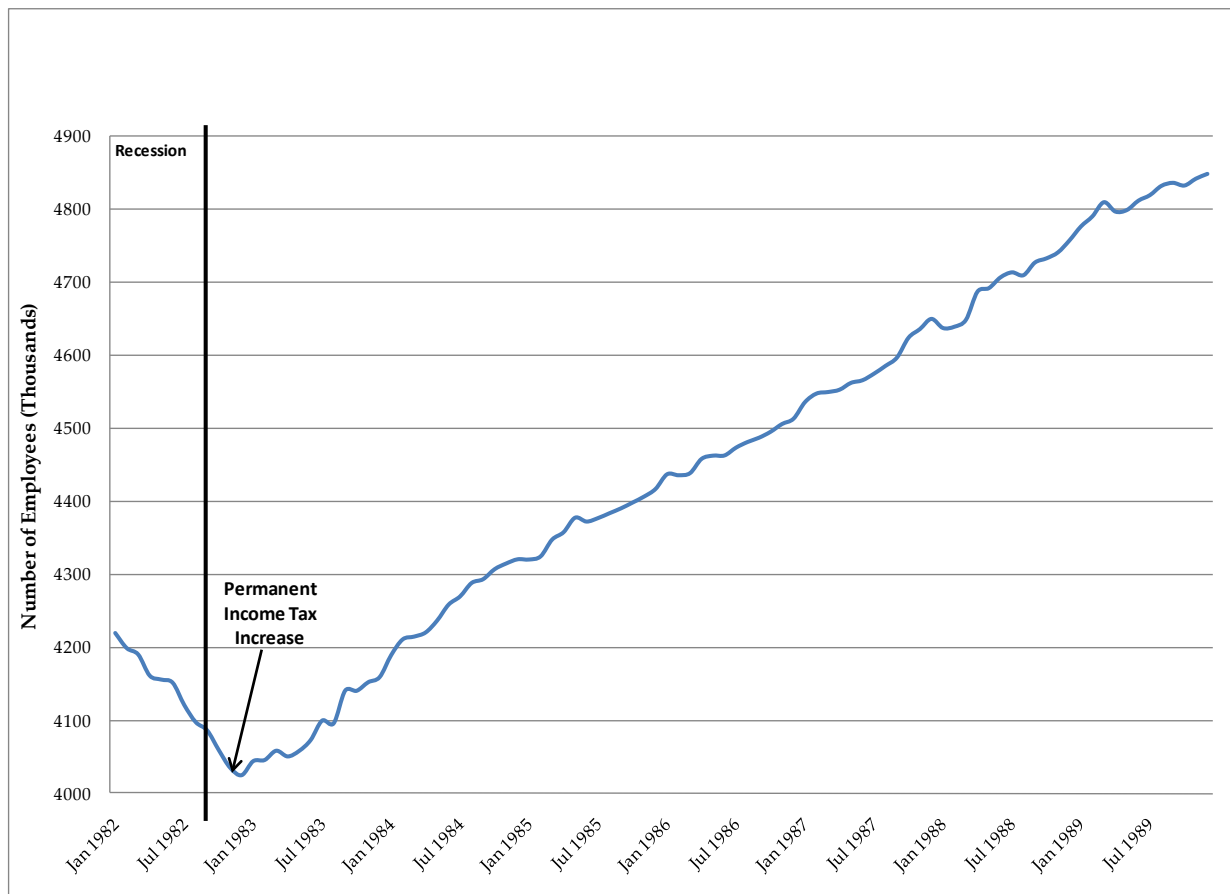
Under Governor Rhodes, the policymakers first turned to a temporary sales tax increase that was made permanent in November, 1981.<sup>4</sup> The next year, the legislature added two temporary income tax brackets with higher rates for those making over \$80,000. The top rate of the income tax was raised to 6.25 percent on incomes over \$100,000; the previous top rate had been 3.5 percent and took effect at \$40,000 of income.

In 1983, Ohio faced a deficit of \$511 million for the fiscal year and a projected shortfall of \$2.5 billion for the next biennium. Governor Celeste responded by calling for a combination of spending reductions (which included cutting Medicaid provider rates and education aid for school districts), delayed implementation of new social service programs (such as parity in per-pupil funding for students with developmental disabilities and establishment of the “Workfare” program to move welfare recipients to jobs), and an income tax increase.<sup>5</sup>

In response to Governor Celeste’s proposal, the income brackets were made permanent and rates were raised. The rate on the top bracket for incomes over \$100,000 peaked at 9.5 percent in 1984 before falling to 6.9 percent in the late 1980s.

In the seven years from 1983 to 1989, the Ohio economy added an average of nearly 118,000 jobs per year (Figure 1).

**Figure 1. Ohio Payroll Employment, 1982 – 1989 (seasonally adjusted)**



Source: Bureau of Labor Statistics; The Center for Community Solutions.

**1990s: 7.5 percent bracket added for income over \$200,000**

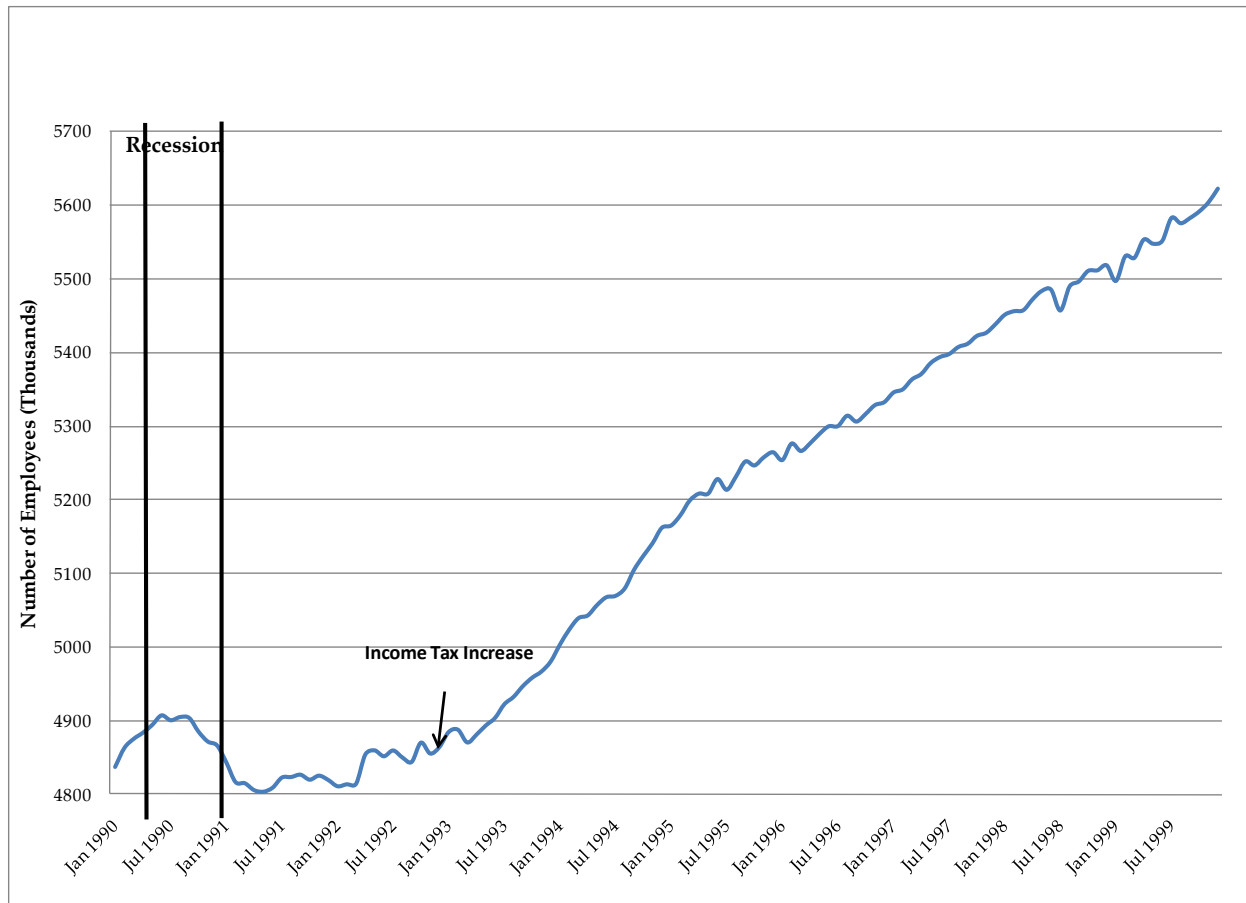
In 1993, under Governor Voinovich, a new top bracket of 7.5 percent on taxable income above \$200,000 was added to the personal income tax.<sup>6</sup> This change followed an intense debate about how to close a budget hole of around \$1 billion. The state also made spending cuts of more than \$600 million in which higher education spending was significantly reduced. The marginal rate on the next lower bracket, for incomes between \$100,000 and \$200,000, remained at 6.9 percent. The state sales tax was extended to

various discretionary services more likely to be purchased by high-income individuals (e.g. lawn care, premium cable television, security services). Some of the tax increases enacted at the time were later repealed by voters (a soda tax) or by the legislature (automobile warranty services).

Again, increasing taxes during the depths of the recession did not hinder the economy's recovery. In fact, Ohio enjoyed robust economic growth. Unemployment fell six out of seven years following the tax increase and was lowered to rates the state had not experienced since the 1960s.<sup>7</sup>

In the seven years from 1993 to 1999, Ohio's economy created an average of 108,000 jobs per year (Figure 2).

**Figure 2. Ohio Payroll Employment, 1990 – 1999 (seasonally adjusted)**



Source: Bureau of Labor Statistics; The Center for Community Solutions

The strong economic recovery buoyed state revenues and lawmakers decided to cut some taxes in the latter half of the 1990s. Starting in 1996, income tax rates were cut, based on an annual formula that determined the amount of revenue left over after filling Ohio's Budget Stabilization (Rainy Day) Fund. The highest rate never dropped below 6.79 percent, a level which is still above the current (2009) top rate of 5.925 percent.

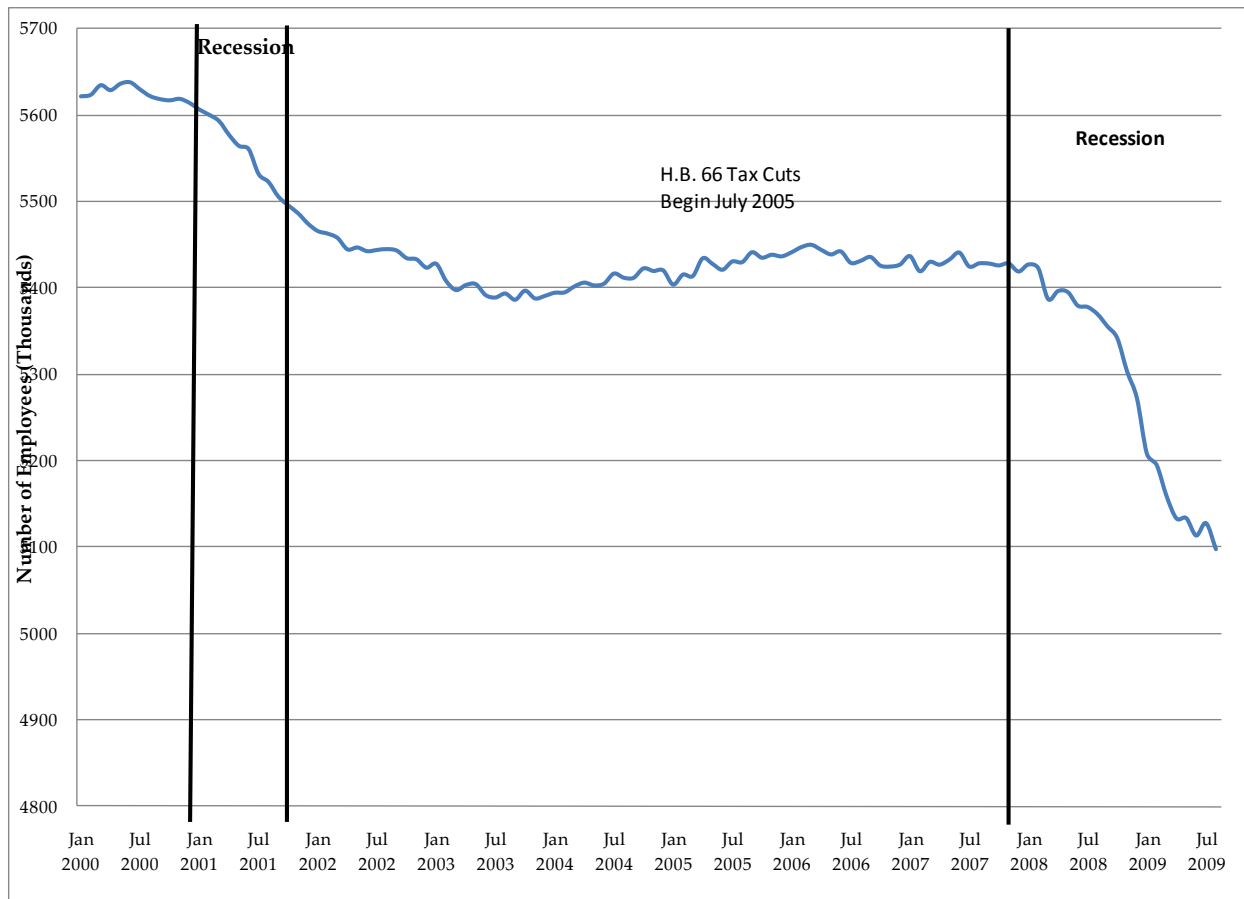
### **2000s: Two Recessions, Little Job Growth**

In the wake of the 2001 recession, income tax rates returned to their previous levels. When this action was insufficient to balance the state budget, lawmakers used the Rainy Day Fund and diverted the state's payments from a national settlement with tobacco companies. In Fiscal Years 2004 and 2005, Governor

Bob Taft, a Republican, proposed and the legislature approved a temporary increase in the sales tax rate to 6 percent from 5 percent and an extension of the tax to additional services. Job growth was small but positive in 2004 and 2005.

A sweeping tax overhaul in 2005 cut income tax rates by a total of 21 percent over five years and also cut business taxes. An economic consulting firm hired by the Taft Administration forecast that Ohio would gain 41,500 jobs by 2009 as a result of the changes, but the economy failed to generate significant job growth even before the onset of the national recession in December, 2007.<sup>8</sup> The most recent peak in employment occurred in the first quarter of 2006. Job losses resumed *after the tax cuts* (Figure 3).

**Figure 3. Ohio Payroll Employment, 2000-2009 (seasonally adjusted)**



Source: Bureau of Labor Statistics; The Center for Community Solutions.

The Ohio House has now passed House Bill 318, which would cancel the final year of the income tax cuts. The governor turned to this option after the Ohio Supreme Court ruled that the plan to put slot machines at Ohio racetracks could be subject to a voter referendum. The income tax increase in House Bill 318 is only for two years. In 2011, rates would return to their current levels in spite of the fact that the state faces the loss of \$4 billion per year in federal fiscal relief and one-time state funds that will not be available in the next budget. In light of the devastating cuts in this budget to basic public services and the enormous revenue gaps that the state will face in the future, income tax rates should be increased even more, particularly on wealthier individuals, and the increase should be made permanent.

Other states, including Wisconsin, New York, New Jersey, and North Carolina, have raised income taxes in this recession to fill part of their budget shortfalls. Maintaining our current policy of cutting services to abused children, the mentally ill, and families who are waiting for emergency assistance will do

permanent damage to our quality of life. There is no more time to wait. The governor and legislature should act now to raise revenue and restore adequate funding to social services.

---

<sup>1</sup> Lucy Dadayan and Donald J. Boyd, "State Tax Revenues Show Record Drop, for Second Straight Quarter," *State Revenue Report No. 77* (Oct. 2009), Rockefeller Institute of Government. Available at [http://www.rockinst.org/pdf/government\\_finance/state\\_revenue\\_report/2009-10-15-SRR\\_77.pdf](http://www.rockinst.org/pdf/government_finance/state_revenue_report/2009-10-15-SRR_77.pdf)

<sup>2</sup> Joe Hallet, "Eventually, governors in Ohio turn to tax hikes." *Columbus Dispatch*, 25 May 2009.

<sup>3</sup> A listing of Ohio's income tax brackets and rates are available from the Ohio Department of Taxation at [http://tax.ohio.gov/divisions/tax\\_analysis/tax\\_data\\_series/historical\\_time\\_series/documents/OHIOINCOMETAXTABLES.pdf](http://tax.ohio.gov/divisions/tax_analysis/tax_data_series/historical_time_series/documents/OHIOINCOMETAXTABLES.pdf).

<sup>4</sup> Ohio Department of Taxation, *Annual Report 1998*, Sales and Use Tax section, p. 109.

[http://tax.ohio.gov/divisions/communications/publications/annual\\_reports/1998\\_Annual\\_Report/Section\\_24.pdf](http://tax.ohio.gov/divisions/communications/publications/annual_reports/1998_Annual_Report/Section_24.pdf)

<sup>5</sup> For a description of the debate at the time, see "Celeste Tax-Boost Proposal Unjustified, Gillmor Says" *Toledo Blade*, 22 February 1983. Available at:

<http://news.google.com/newspapers?nid=1350&dat=19830222&id=ZnkUAAAIBAJ&sjid=vAIEAAAIBAJ&pg=4781,6692934>.

<sup>6</sup> A description of the early 1990s tax changes is contained in Don Berno and Jack L. Whitmore, "Historical Review of State and Local Government Finances," in *Taxation and Economic Development: A Blueprint for Reform in Ohio*, Roy Bahl, ed. (Columbus, OH: Battelle Press, 1996), pp. 159 – 219.

<sup>7</sup> The Ohio Legislative Service Commission, *Ohio Facts 2001*, January 2001.

<http://www.lbo.state.oh.us/fiscal/publications/biennial/ohiofacts/JAN2001/OhioFacts2001.pdf>

<sup>8</sup> Jon Honeck, *The 2005 Tax Overhaul and Ohio's Economy*. Policy Matters Ohio (January 2009). Available at [www.policymattersohio.org/2005TaxOverhaul.htm](http://www.policymattersohio.org/2005TaxOverhaul.htm), see pp. 8-9.