Rebalancing the Alabama Economy for Sustained Growth

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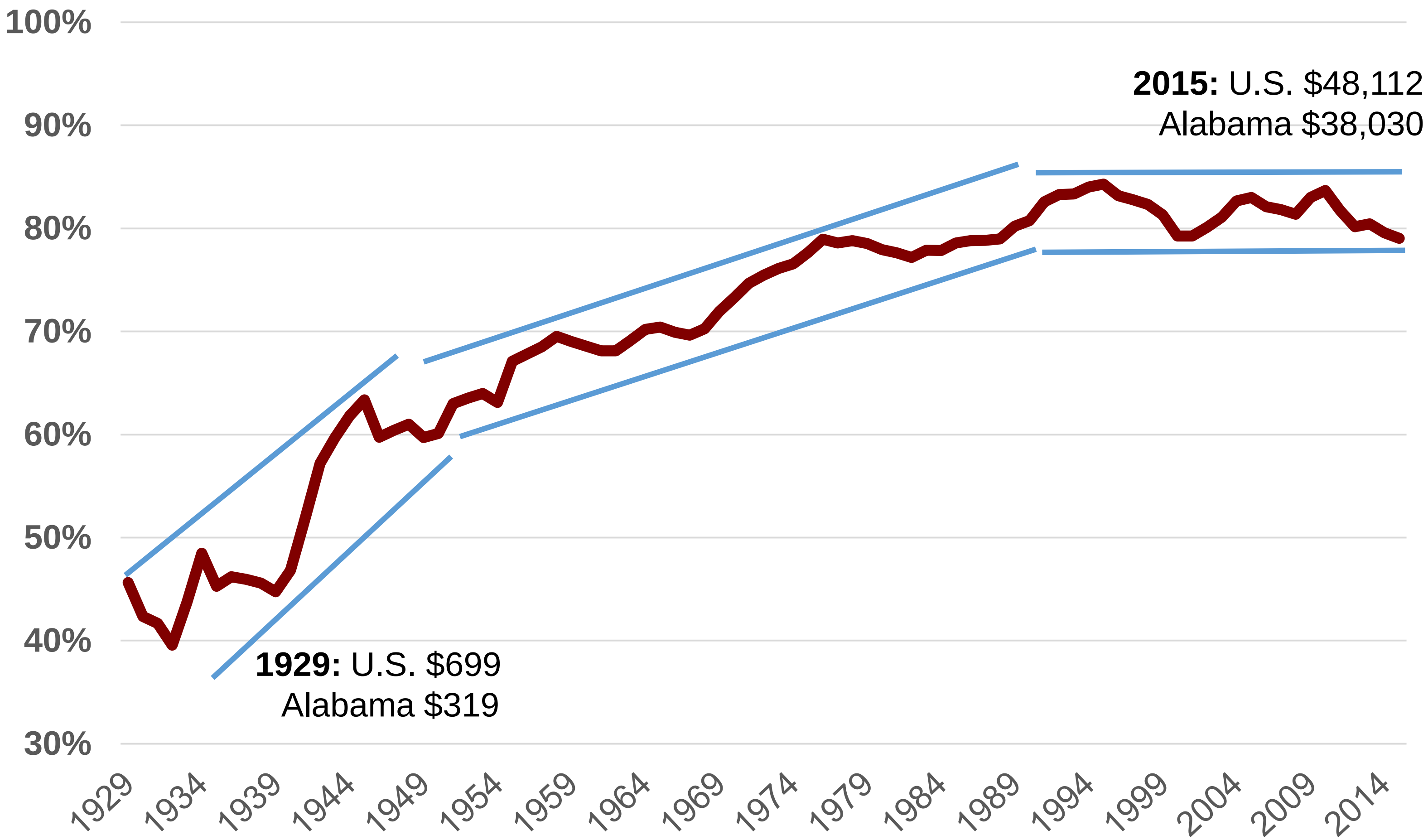
Per Capita Income: Alabama to U.S. Ratio



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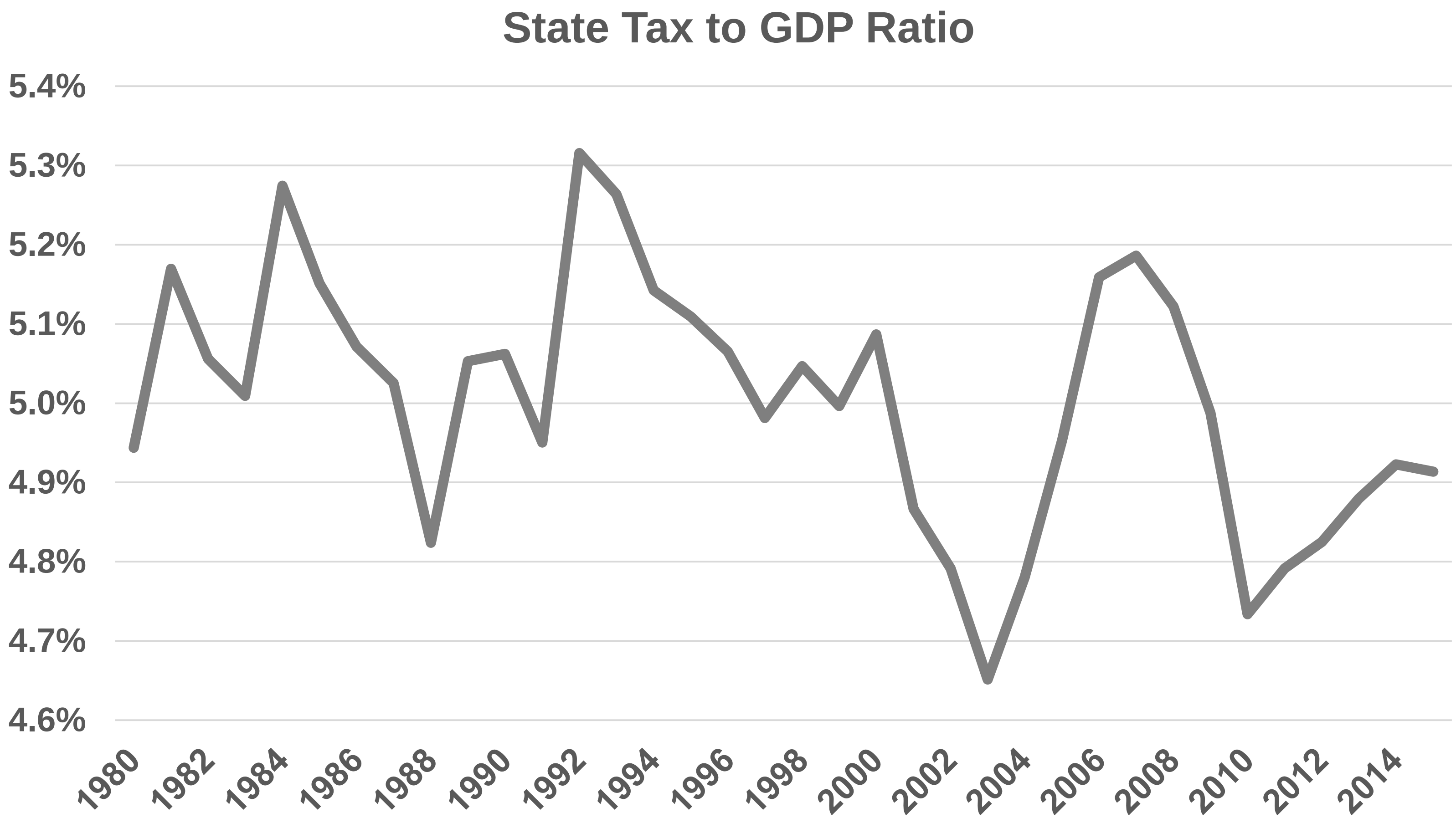
Alabama Structural Imbalance: Declining Public Sector Spending



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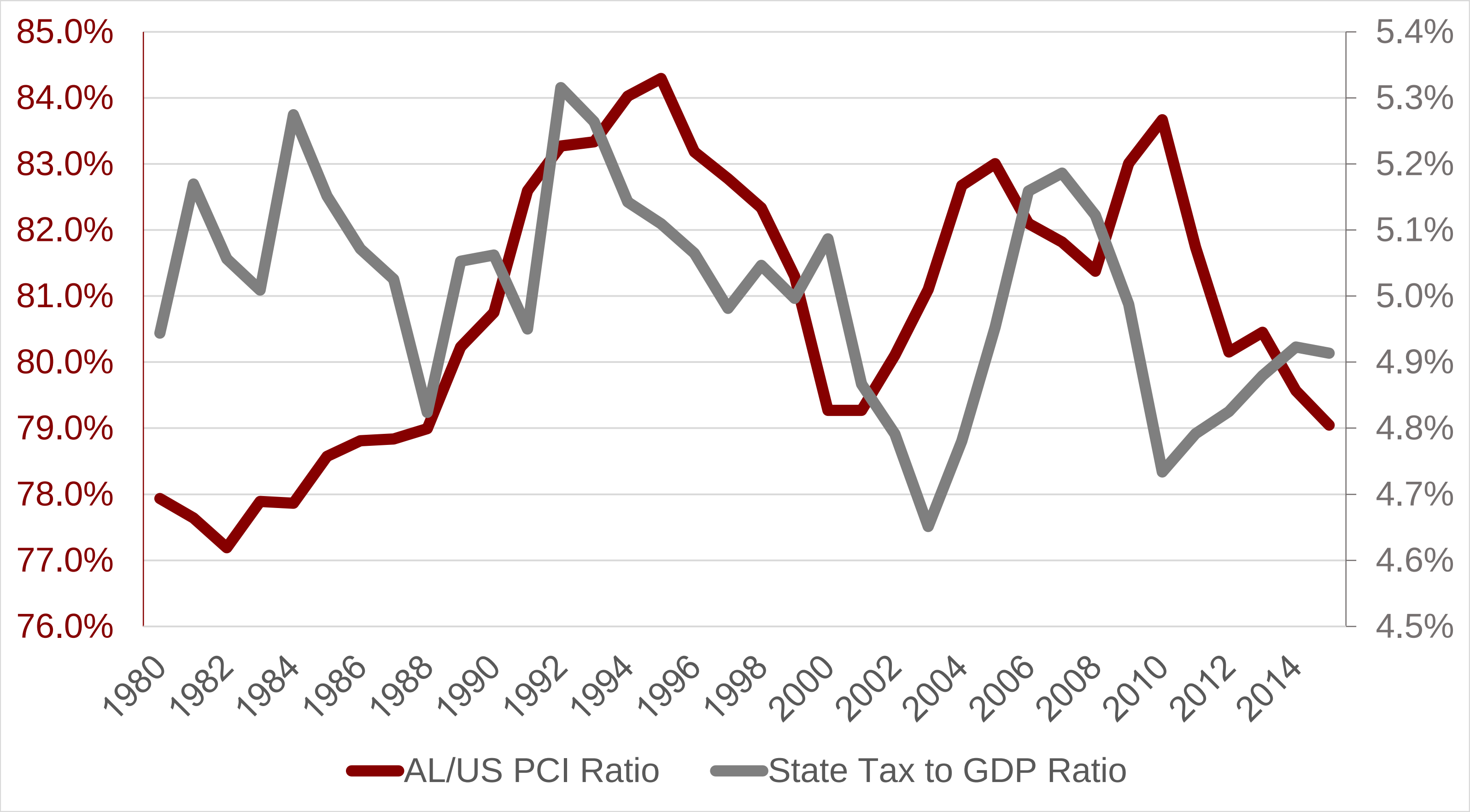
Alabama Structural Imbalance: Declining Public Sector Spending is Holding Back Growth



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Growing the Alabama Economy

- Sustained and optimal economic growth for Alabama will require rebalancing by raising the public spending share of GDP
- **Goal**: Broad-based economic growth for all of Alabama with a focus on increasing the ratio of state to national per capita income
- **Education is key (no economic development otherwise)**
- **Healthcare too**
- **A better tax system is needed** because what we currently have
  - raises inadequate revenue
  - is regressive
  - is inefficient in both collection and use
- **Alabama needs BOTH tax and budget reform**

Suggestions for a Better Tax System to Support Optimal Economic Growth for Alabama

- Acknowledge scale of problem; about $2.0 billion (1% of GDP) is needed
  - We have to properly define the problem before we can solve it. From the perspective of "optimality" or asking what is best for Alabama, funds are needed to address expected/projected budget shortfalls as well as to properly address workforce development (education and other programs), infrastructure improvements, and economic development incentives. The economy is a system of interacting public and private sectors; a "healthy" public sector enables the private sector and economy as a whole to grow in the best way possible.
  - Removal of federal income tax deduction: $700-850 million
  - Lowering sales tax rate and broadening base (+20%): $430 million
  - Raising state property tax from 6.5 mills to 13 mills: $370 million
  - Instituting road use fees (1-cent per mile): $680 million
  - Use $400-500 million for incentives and budget reconciling

Economic Impact of $2 Billion Rebalancing

- Net effects indicate that rebalancing is worth it.

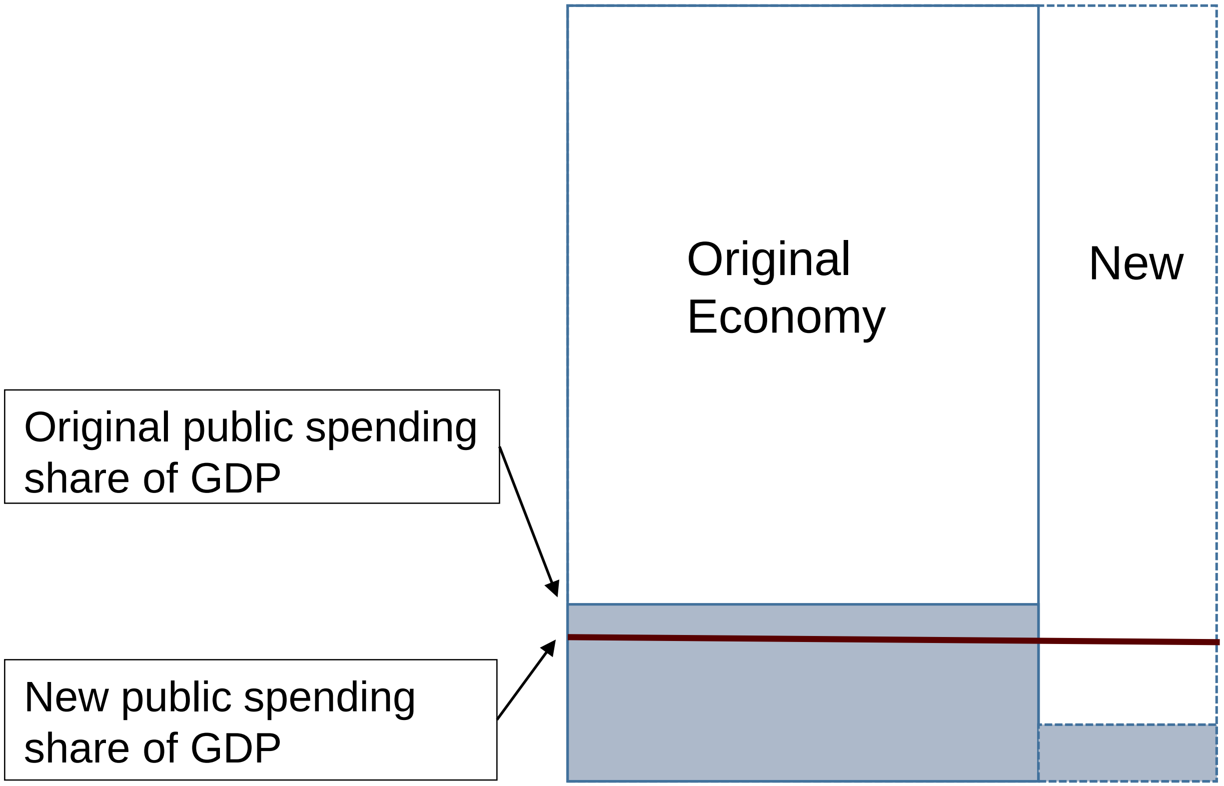
$ Millions	Consumption Reduction	Government Spending	Net Effect
Output	**($3,953)**	**$4,981**	**$1,027**
GDP	**($1,956)**	**$2,465**	**$508**
Earnings	**($1,110)**	**$1,526**	**$416**
Employment (jobs)	**(19,842)**	**29,896**	**10,054**

Rationale for Better Tax System Suggestions

- Reduce tax expenditures (especially, federal income tax deduction)
  - Although some people might disagree, it is a fact that eliminating or reducing tax deductions (also called tax expenditures) is not the same as raising taxes; it is rather a removal of subsidies. Deductions are essentially subsidies that are instituted at some point and enable those who can take advantage of them to pay lower state taxes than they would otherwise pay. The removal or elimination of deductions just takes taxpayers back to what they would or should have paid without the allowed subsidy. So getting rid of them is not the same as raising taxes.
  - Economic development incentives are investments which must be accompanied by new revenue (as suggested in the previous slide) or borrowing. Selectivity is vital as the investments MUST be in projects that will pay off; these projects HAVE to provide jobs that pay higher than existing average wage. **Incentive programs should be evaluated up front and periodically to ensure that they are worthwhile**.

Use of Incentives Requires New Revenue

- Without new revenue, incentives unbalance the economy by reducing the public spending share of GDP



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Rationale for Better Tax System Suggestions

- Broaden tax base; lower sales tax rate and apply to services too
  - This is needed because the state's economic structure has been changing. The service sector is the larger and faster-growing part of the economy as consumers spend much more on services than on goods. Goods production and services provision use up public goods/services for which revenues are needed. As such it is important to generate revenues from both goods and services, not just goods; sales tax collections used to be higher than income tax collections but the reverse is true now.
- Raise state property tax
  - The state's tax structure is seriously unbalanced and inefficient in both collection and use with the currently small property tax receipts constituting a significant part of the problem.

Rationale for Better Tax System Suggestions

- Institute road use fees
  - The gas tax is insufficient for road infrastructure needs and is also much less useful for raising revenues to address those needs. A fee based on vehicle miles traveled (VMT) or road use is the proper basis for such revenue.
  - This can be paid annually at tag renewal with varying fees for different vehicle types (e.g., using axle or weight classes). For example, a one-cent per mile fee for cars would generate $100 for 10,000 miles traveled a year; VMT can be determined from reading odometers.
  - The gas tax need not be phased out as its significance will fall naturally over time and it will help with getting some revenue from vehicles that are not domiciled in Alabama. To ensure that revenues match road infrastructure expenditure needs, the VMT fee can be (i) indexed to inflation or (ii) assessed and adjusted appropriately every few years.

Questions, Comments, Discussions?

The individual appears for an instant, joins the community of thought, modifies it and dies; but the species, that dies not, reaps the fruit of his ephemeral existence.

\- A.S. Byatt, ***Possession***

Thank You

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