

This edition is the 2011 SBTCI and represents the tax climate of each state as of July 1, 2010, the first day of the standard 2011 fiscal year.

The Best and Worst Business Tax Climates

The ten best states in the Tax Foundation's 2011 State Business Tax Climate Index are as follows:

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| 1. South Dakota | 6. Montana |
| 2. Alaska | 7. New Hampshire |
| 3. Wyoming | 8. Delaware |
| 4. Nevada | 9. Utah |
| 5. Florida | 10. Indiana |

It is obvious that the absence of a major tax is a dominant factor in vaulting these ten states to the top of the rankings. Property taxes and unemployment insurance taxes are levied in every state, but there are several states that do without one or more of the major taxes: the corporate tax, the individual income tax, or the sales tax. Wyoming, Nevada and South Dakota have no corporate or individual income tax; Alaska has no individual income or state-level sales tax; Florida and Texas have no individual income tax; and New Hampshire, Delaware, Oregon and Montana have no sales tax.

The lesson is simple; a state that raises sufficient revenue without one of the major taxes will, all things being equal, out-compete those states that levy every tax in the state tax collector's arsenal.

The ten worst states in the SBTCI are as follows:

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| 41. North Carolina | 46. Ohio |
| 42. Rhode Island | 47. Connecticut |
| 43. Minnesota | 48. New Jersey |
| 44. Maryland | 49. California |
| 45. Iowa | 50. New York |

New York scores at the bottom by having the third worst individual income tax, ninth worst sales tax, and worst property tax. Rhode Island has improved from 44th to 42nd but still has the worst unemployment tax system and third worst property tax system. Connecticut managed a remarkable drop—from 38th in last year's index to 47th in this year's—mostly by creating a new “millionaire's bracket” on the individual income tax. New Jersey has broken a three-year streak of having the worst business tax climate in the country, improving to 48th. The states in the bottom ten suffer from the same afflictions:

complex, non-neutral taxes with comparatively high rates.

A detailed description of each component index, each sub-index, and their various components is presented later in the paper, and those states that score especially well or poorly on each component are discussed to provide guidance on the changes that each state might well contemplate.

A Review of the Economic Literature

Economists have not always agreed on how individuals and businesses react to taxes. As early as 1956, Charles Tiebout postulated that if citizens were faced with an array of communities that offered different types or levels of public goods and services at different costs or tax levels, then all citizens would choose the community that best satisfied their particular demands, revealing their preferences by “voting with their feet.” Tiebout's article is the seminal work on the topic of how taxes affect the location decisions of taxpayers.

Tiebout suggested that citizens with high demands for public goods would concentrate themselves in communities with high levels of public services and high taxes while those with low demands would choose communities with low levels of public services and low taxes. Competition among jurisdictions results in a variety of communities, each with residents that all value public services similarly.

However, businesses sort out the costs and benefits of taxes differently from individuals. To businesses, which can be more mobile and must earn profits to justify their existence, taxes reduce profitability. Theoretically, then, businesses could be expected to be more responsive than individuals to the lure of low-tax jurisdictions.

No matter what level of government services individuals prefer, they want to know that public goods and services are provided efficiently. Because there is little competition for providing government goods and services, ferreting out inefficiency in government is notoriously difficult. There is a partial solution to this “information asymmetry” between taxpayers and government employees: “Yardstick Competition.” Shleifer

NEW JERSEY

New Jersey moved up two spots this year from the lowest-ranked tax climate to 48th best. This may be small consolation for New Jersey taxpayers, but after four consecutive years ranking 50th, any improvement is welcome. The principal change was elimination of the top two personal income tax brackets when the governor vetoed a measure that would have extended the existing, higher rates. After the veto, the top tax rate fell from 10.75% to 8.97%.