



Media Contact:
Jessica Fletcher
Communications Manager
Kentucky Chamber
jfletcher@kychamber.com
502-848-8731

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Holding the line on taxes improves Kentucky's business ranking

An op-ed by Dave Adkisson, president and CEO, Kentucky Chamber of Commerce

Businesses make location and expansion decisions based on several factors. Among them: the availability of a skilled workforce, education quality, proximity to markets, labor issues and, of course, taxes. It is in that last category that Kentucky has made significant progress in recent months – even if the change hasn't generated headlines across the state.

The 2010 State Business Tax Climate Index from the Tax Foundation ranks Kentucky 20th in the nation on this important indicator. The ranking is significant in its own right – putting Kentucky in the top half of states. But it is even more noteworthy because of the change it represents: Kentucky jumped up from No. 34 in the 2009 index – the greatest gain of any state in the nation.

As the Tax Foundation pointed out:

"Kentucky rose through the ranks faster than any other state this year, up 14 spots from 34th best in the 2009 Index to 20th this year. That might be surprising to Kentuckians who have not seen much change in their tax system, but sometimes standing fast is a virtue. Many economically damaging changes were enacted in other states that previously ranked better than Kentucky. This was particularly true in the personal income tax, where Kentucky saw gains as other states added more brackets with higher rates."

Kentucky's lawmakers are to be commended for holding the line on new or increased taxes during these tough economic times. Not only did their leadership heighten the state's national profile, it also will better position Kentucky and its employers for recovery. The action indicates that our legislators understand what the Tax Foundation describes in the latest Business Tax Climate Index as the two rules of improving a state's competitiveness:

1. Taxes matter to business. Business taxes affect business decisions, job creation and retention, plant location, competitiveness, the transparency of the tax system, and the long-term health of a state's economy. Most importantly, taxes diminish profits. If taxes take a larger portion of profits, that cost is passed along to either consumers (through higher prices), workers (through lower wages or fewer jobs), or shareholders (through lower dividends or share value). Thus, a state with lower tax costs will be more attractive to business investment, and more likely to experience economic growth.
2. States do not enact tax changes (increase or cuts) in a vacuum. Every tax law will in some way change a state's competitive position relative to its immediate neighbors, its geographic region, and even globally. Ultimately it will affect the state's national standing as a place to live and to do business. Entrepreneurial states can take advantage of the tax increases of their neighbors to lure businesses out of high-tax states.

Kentucky's 20th-place ranking improves its position relative to surrounding states. Ohio, unchanged from its 2009 position of 47th, is among the worst-ranked states in the nation. The performance of other neighbors:

- Illinois: down from 23rd to 30th
- Indiana: up from 14th to 12th
- Missouri: consistent at 16th

- Tennessee: down from 17th to 22nd
- West Virginia: down from 36th to 37th

The improved overall ranking doesn't mean that Kentucky has a consistently strong performance in all business taxes, of course. The index is based on several components that are weighted based on how much they vary from state to state. Personal income tax is the most heavily weighted, followed by sales, corporate income, property and unemployment insurance.

Kentucky's national ranking on the individual components for 2010 was:

- Corporate income tax: 42
- Personal income tax: 32
- Sales tax: 7
- Unemployment insurance tax: 36
- Property tax: 19

These figures show that the state, while making progress, still has room for growth in creating a business-friendly environment when it comes to taxation.