December 30, 2011

Governor Mary Fallin
212 State Capitol
Oklahoma City, OK 73105

President Pro Tempore Brian Bingman
422 State Capitol
Oklahoma City, OK 73105

Speaker Kris Steele
401 State Capitol
Oklahoma City, OK 73105

Dear Governor Fallin, President Pro Tempore Bingman and Speaker Steele:

As Co-chair of the Task Force on Comprehensive Tax Reform, I am pleased to provide to you with the report required pursuant to Senate Joint Resolution 61 (2010 Legislative Session) to study comprehensive reform for Oklahoma's tax system. The Task Force focused on three primary goals:

1. Resolution of the issues surrounding taxation of intangible properties;
2. Changes to our tax code which would lower income tax rates and broaden the base of taxpayers to stimulate our economy and grow our tax revenue base for government priorities; and
3. Development of a framework for Oklahoma to become a "no-income tax" state.

Thanks to the hard work, dedication and intensive collaboration of the members of the Task Force, the following report provides recommendations to address each of the goals listed above. In addition to four public hearings, a large number of Task Force members put in numerous hours of thought and effort during several work sessions to discuss the advantages and disadvantages of the ideas and concepts that were presented to us by guest experts at our hearings. Our work proceeded in a very inclusive manner to make sure that adequate consideration was given to all participants in this process.

As you and members of the Legislature consider these proposals, we hope that the taxpayers of Oklahoma will be your main priority. The non–partisan Tax Foundation has rated Oklahoma's overall tax structure number 30 out of the 50 states when assessing our job creation environment. We can and must do better to shift our tax code away from special interest groups who benefit from obsolete and ineffective tax preferences and toward hardworking Oklahomans who deserve to keep more of their hard earned income. If done correctly, tax reform will lower tax rates and broaden the base of taxpayers. This in turn will raise the standard of living for all Oklahomans and also generate an increase in government revenues for top priorities such as education and roads and bridges.

We believe that if the following recommendations are put into action, tremendous economic benefit will result for the state of Oklahoma for years and years to come. We hope and respectfully ask that you and the Legislature give special time and attention to this report and our recommendations.

Task Force members in support of this Final Report and Recommendations:

Senator Mike Mazzei, Task Force Co-Chair
Representative David Dank, Task Force Co-Chair

Senator Rick Brinkley
Secretary of State Glenn Coffee
Director of State Finance Preston Doerflinger
Bryan Gonterman
Tax Commission Chairman Thomas Kemp
Kirby Lehman
Marty Lewis
Charles Mills
County Assessor Wade Patterson
Dan Ramsey
Dana Weber
Representative Harold Wright

TASK FORCE ON COMPREHENSIVE TAX REFORM (SJR 61)

List of Members

Name	Appointing Authority	SJR 61 Qualifications
Senator Mike Mazzei, ***Co-Chair***	Senate	Chair of Senate Finance Committee
Representative David Dank, ***Co-Chair***	House	Chair of House Revenue and Taxation Subcommittee of the Appropriations and Budget Committee
Senator Rick Brinkley	Senate	Vice-Chair of Senate Finance Committee
Secretary Glenn Coffee	Senate	Member of Senate (at time of original appointment)
Kirby Lehman	Senate	Superintendent or Board Member of Elementary or Independent School District
Russell Phillips	Senate	Representing the Energy Industry
Dan Ramsey	Senate	Representing the Insurance Industry
Mark Headley	House	Representing Statewide Organization of Business
Albert “Kell” Kelly	House	Representing Banking Industry
Marty Lewis	House	Superintendent or Board Member of Elementary or Independent School District
Representative Harold Wright	House	Vice-Chair of House Revenue and Taxation Subcommittee of the Appropriations and Budget Committee (original appointment)
Richard Dowell	Governor	Representing Small Business
Bryan Gonterman	Governor	Representing Technology Industry
Don Millican	Governor	Member at Large
Charles Mills	Governor	Representing Small Business
Wade Patterson	Governor	County Assessor
Nicholas Tricinella	Governor	Representing the Energy Industry
Dana Weber	Governor	Representing a Statewide Organization of Business
Preston Doerflinger	Statutory	Office of State Finance
Thomas Kemp	Statutory	Oklahoma Tax Commission

TASK FORCE ON COMPREHENSIVE TAX REFORM

INTRODUCTION

The Task Force on Comprehensive Tax Reform was created in Senate Joint Resolution 61 during the 2010 legislative session. The Task Force was given a broad mandate to, "recommend amendments to the Business Activity Tax Code, to review the different types of tax imposed on businesses and individuals in this state and to develop recommendations and proposed legislation to provide increased simplification and fairness in the tax structure of the state." The legislation provided for 21 members, appointed by the Governor, Senate and House. The group includes members of the State Legislature, other state and local officials, and members of the business and education communities. This final report is required to be submitted the Governor, President Pro Tempore and Speaker on or before January 1, 2012.

BACKGROUND

The Task Force held four public meetings for the purpose of hearing testimony and gathering information related to the Task Force's mission.

The first meeting was held on September 15, 2011. The purpose of this meeting was to receive input from a variety of speakers representing local and national perspectives. The Task Force heard from the following:

- Mandy Rafool, Fiscal Affairs Program, National Conference of State Legislatures;
- Michael Carnuccio, President, Oklahoma Council of Public Affairs; and
- David Blatt, Director, Oklahoma Policy Institute.

Ms. Rafool provided the Task Force with an overview of: state tax sources, the tax structures of Oklahoma's surrounding states and the state of North Dakota and recent comprehensive tax reform efforts in other states. The information provided by Ms. Rafool showed the extent to which each state relies upon various tax types to fund state and local government and the breakdown of state and local business tax collections. She highlighted tax reform efforts in Ohio, Texas and Michigan.

The presentations by Mr. Carnuccio and Mr. Blatt were structured in response to specific questions posed by the Task Force. The response of each of the speakers is summarized below.

1. Should the Oklahoma Constitution be amended to exempt all intangible personal property from the ad valorem tax?

Mr. Carnuccio: Yes, due to the disadvantages and problems inherent in taxing intangible personal property.

Mr. Blatt: No, due to the substantial revenue loss which could result from property which is currently subject to ad valorem taxes (intangible personal property of centrally-assessed entities). The optimal solution is to limit the tax levy to such property (the status quo ante).

2. Should Oklahoma tax business activity with a BAT, a corporate income tax, and a franchise tax as done under the present system or should one of those taxes be levied in place of the others?

Mr. Carnuccio: The BAT and franchise taxes penalize activity and production. If business activity must be taxed at all, the corporate income tax is the least problematic.

Mr. Blatt: The corporate income tax is an important component of an adequate and fair system, but should be strengthened by adopting combined reporting. In addition, Oklahoma should retain some form of broad-based, low rate assessment calculated on investment or gross receipts.

3. Should Oklahoma enact stricter enforcement of taxes for online sales?

Mr. Carnuccio: Oklahoma should continue to justly collect taxes for online sales but not in a way that undermines the spirit of the *Quill* decision.

Mr. Blatt: Mr. Blatt explained the challenges of taxing online sales and the estimated revenue loss which results. He noted that some states have enacted provisions to clarify the interpretation of "nexus".

4. *Should Oklahoma seek to reduce its income tax rate from its current level at5.25%? If so, what do you believe is the ideal income tax threshold?*

Mr. Carnuccio: Yes, individual income taxes should be eliminated completely over a period of seven to ten years.

Mr. Blatt: No, income tax is vital for an adequate and balanced system. The amount of all tax collections represented by income tax has fallen since 2005.

5. How do you accomplish an income tax reduction and maintain revenue neutrality?

Mr. Carnuccio: By eliminating all income tax credits and deductions and using resulting revenue gains to phase out the income tax.

Mr. Blatt: In 2001, this proposition was considered and then-Governor Keating initially proposed a 5.9% gross receipts tax as a substitute for income tax and sales tax on groceries.

6. Should Oklahoma eliminate the income tax to be more competitive in a 21st century economy?

Mr. Carnuccio: Yes, in the nine states without income taxes this has resulted in higher GDP growth, job growth and total state tax receipts.

Mr. Blatt: No, income tax is vital for our system and slashing the tax is not the right path for economic growth. Research has shown that investment decisions are driven more by a well-trained, productive workforce and strong infrastructure than by state and local tax rates.

7. If you could design your ideal tax system for Oklahoma, how would it be structured and why?

Mr. Carnuccio: The system would have no personal income tax, other main tax types (sales, corporate income and premium taxes) would be broad-based and at the lowest possible rate. Local taxes would include sales and property taxes only.

Mr. Blatt: Five ideas for tax reform include: (1) limit tax incentives; (2) limit itemized income tax deductions; (3) strengthen sales tax; (4) allow higher taxes on commercial property; and (5) provide broad-based income tax cuts.

The second meeting was held on October 20, 2011. The purpose of this meeting was to receive input from representatives of the state and local business community. The Task Force heard from the following:

- Chris Benge, Sr. Vice President, Government Affairs, Tulsa Metro Chamber of Commerce;
- Scott Meacham, Board Member, Oklahoma State Chamber of Commerce; and
- Wes Stuckey, President, Ardmore Chamber of Commerce

Each of the speakers addressed the issues raised in the questions posed by the Task Force. The response of each of the speakers is summarized below.

1. Should the Oklahoma Constitution be amended to exempt all intangible personal property from the ad valorem tax?

Mr. Benge: If the failure to do so would result in taxing previously-untaxed intangible personal property, it would need to be done to keep from creating a huge new tax burden.

Mr. Meacham: New taxation of intangibles could pose a serious threat to businesses large and small. However, the State Chamber also believes government supported services which are currently receiving ad valorem revenue from the taxation of intangibles are important.

Mr. Stuckey: The importance of property tax in business development depends on the type of business. When property tax is an important issue to a relocating business, Oklahoma compares very favorably to Texas.

2. Should Oklahoma tax business activity with a BAT, a corporate income tax, and a franchise tax as done under the present system or should one of those taxes be levied in place of the others?

Mr. Benge: The most important thing is to simplify and streamline the tax code in a way that encourages business growth.

Mr. Meacham: The most advantageous move would be to roll all of the taxes into as few as possible. The type of tax can be misleading. For example, Texas has a franchise tax which is based on income, but no “income tax”.

Mr. Stuckey: There is no silver bullet answer to the best way to tax business activity because it depends on the way each business is structured. Our income tax is a stable source of revenue needed to fund state services. Credits and exemptions could be eliminated to reduce the top rate.

3. Should Oklahoma enact stricter enforcement of taxes for online sales?

Mr. Benge: The Tulsa Chamber supports stricter enforcement of sales and use tax as a way to help brick and mortar businesses compete with online sales from out of state. They appreciate last year's legislative efforts to address this issue.

Mr. Meacham: All taxes that are due by law should be collected so Oklahoma businesses are not put at a disadvantage. Determinations about online sales are difficult due to interpretation of the *Quill* decision and to actions like those taken by Amazon.

Mr. Stuckey: Broadening the tax base to include more services has potential for our state. We have an enforcement problem in some areas where a cash economy exists and sales are underreported.

4*. Should Oklahoma seek to reduce its income tax rate from its current level at5.25%? If so, what do you believe is the ideal income tax threshold?*

Mr. Benge: The Tulsa Chamber would support anything that encourages the creation and development of more capital in the state but believes this must be balanced with the need to maintain government programs and services which are also vital to economic growth.

Mr. Meacham: If enough tax preferences are eliminated, the state could reduce its top rate to as much as 3%.

Mr. Stuckey: Oklahoma is very competitive when it comes to overall tax burden. Reducing tax preferences might allow for a lower rate but this is only one of a host of factors which businesses use to determine where to locate or expand. The relative importance of the top income tax rate depends on the type of business and the value they place on that over many other factors. A business locating a branch plant may care less about income tax levels than one locating a corporate headquarters.

5. How do you accomplish an income tax reduction and maintain revenue neutrality?

Mr. Benge: Although they would support a revenue neutral income tax rate reduction they urge caution that it is not accomplished by shifting tax burden to business.

Mr. Meacham: Revenue neutrality will only be successful if it is not a reallocation onto the backs of business. A shift to greater reliance on sales tax could be problematic to certain businesses in particular. Tax expenditures which are "give-aways" should be scrutinized and dynamic revenue forecasting should be used.

Mr. Stuckey: There is no silver bullet solution. We must be able to fund state services.

6. Should Oklahoma eliminate the income tax to be more competitive in a 21st century economy?

Mr. Benge: Income tax is only one of the factors important to business growth and development. Elimination of the tax would have to be balanced in such a way that other important factors do not suffer.
Mr. Meacham: The state will lose business and jobs if it eliminates too much of the revenue source which supports government services like education.

Mr. Stuckey: Getting rid of the income tax might not have the expected impact on economic development because there are many other very important issues for economic growth and development.

7. If you could design your ideal tax system for Oklahoma, how would it be structured and why?

Mr. Benge: The system would be designed to attract and retain capital and maintain our pro-growth atmosphere and our low-tax status.

Mr. Meacham: An ideal system would appropriately balance the three primary sources of revenue – income, sales and property tax – and would be much simpler than our present system.

Mr. Stuckey: Because economic development depends highly on the type of business being recruited and its particular needs, an ideal system is difficult to determine. The most important thing is to have a state that is known for excellence.

The third meeting was held on November 17, 2011. Presenters included four economists who provided the Task Force members with perspectives on tax reform. The Task Force heard from the following:

- Dr. Larkin Warner, Economist and Regents Professor Emeritus, Oklahoma State University;
- Dr. Alexander Holmes, Regents Professor of Economics and Department Chair, University of Oklahoma;
- Dr. Mickey Hepner, Dean, College of Business Administration, University of Central Oklahoma; and
- Dr. Noel Campbell, Associate Professor of Economics, University of Central Arkansas

Dr. Warner and Dr. Holmes were asked to comment on a tax reform study they and others authored in 2001 at the request of the Governor and legislative leaders. Their final report was entitled, "Revenue-Neutral Tax Reform for Oklahoma: Issues and Options". Dr. Warner urged the group to be aware of three particular challenges in developing tax policy:

1. Identify your goals and how you plan to achieve them. He noted the difficulty in making tax policy under the constraints of Article X, Section 33, which limits the ability of the Legislature to enact tax increases (commonly referred to as "State Question 640").
2. Make policy using the overall tax structure, not just one aspect or tax type.
3. Look at revenue from the federal government as part of the budget picture. This is likely to change and will have an impact on state revenue and budget decisions.

Dr. Warner also briefly discussed the principles of a good tax system, as described in the 2001 report. Dr. Holmes reflected on some of the constraints to creating the ideal state tax system. Those included: the constitutional limit on tax increases, particular qualities of certain tax types (e.g. volatility of gross production tax), tax competition between various levels of government and equity issues. Holmes suggested that when policymakers look at all of the state's primary state tax sources, it does not make sense to eliminate income tax unless government stops providing or provides less government services and eliminates tax incentives.

Dr. Mikey Hepner and Dr. Campbell were asked to respond to the seven questions posed by the Task Force members. Their responses are summarized below.

1. Should the Oklahoma Constitution be amended to exempt all intangible personal property from the ad valorem tax?

Dr. Hepner: Yes, because the outcome of the Court ruling creates a competitive disadvantage for public service companies, which is contrary to optimal tax policy. In addition, such a tax could cause a migration of firms which have valuable intellectual property.

Dr. Campbell: Yes, accurate valuation is difficult because there is not enough market data for proper comparisons.

2. Should Oklahoma tax business activity with a BAT, a corporate income tax, and a franchise tax as done under the present system or should one of those taxes be levied in place of the others?

Dr. Hepner: The ideal approach is to rely on a reformed corporate income tax and eliminate the franchise tax. In Oklahoma, corporate income tax is determined using the "three-factor formula", where equal weight is given to payroll, property and sales. Hepner believes the formula should be modified and a "single sales factor" should be used.

Dr. Campbell: Oklahoma should maintain the corporate income tax and eliminate the franchise and BAT tax.

3. Should Oklahoma enact stricter enforcement of taxes for online sales?

Dr. Hepner: If possible, yes because brick and mortar businesses in the state are at a disadvantage. However, this could lead some retailers to reduce their investments and business relationships in the state.

Dr. Campbell: It depends upon the marginal benefit and cost associated with stricter enforcement. In Colorado, some e-retailers left the state as a result of increased enforcement efforts.

4. *Should Oklahoma seek to reduce its income tax rate from its current level at5.25%? If so, what do you believe is the ideal income tax threshold?*

Dr. Hepner: No, the impact would be relatively small and Oklahoma's personal income taxes are currently below the national average. A better strategy would be to reduce sales taxes, which are above the national average.

Dr. Campbell: Campbell was unwilling to take a position on this question citing his lack of background knowledge on Oklahoma finances and general opinion about the use of personal income tax as a revenue producer.

5. How do you accomplish an income tax reduction and maintain revenue neutrality?

Dr. Hepner: This would require significant revenue increases in other tax types. There several alternatives, each with advantages and disadvantages. One is to expand the sales tax base by including services and raise the tax rate. The other would be to increase property taxes, possibly by levying a state property tax.

Dr. Campbell: There are several paths to revenue-neutrality. One is to enact offsetting changes in the tax code, either by increasing the rate on another tax base or by levying a new tax. Another possibly is to rely upon the increased economic activity and productivity which may result from the income tax reduction. These assume that government spending will decrease to the optimal level – spending and taxes cannot be separated.

6. Should Oklahoma eliminate the income tax to be more competitive in a 21st century economy?

Dr. Hepner: No, the sales tax rate is a more pressing problem and our economy is already competitive. Also, elimination of the income tax could shift more tax burden towards middle-and lower-income families.

Dr. Campbell: Oklahoma should seriously consider eliminating the income tax but not without carefully managing future expenditures. Eliminating income tax could unleash latent innovation, entrepreneurship and venture creation.

7. If you could design your ideal tax system for Oklahoma, how would it be structured and why?

Dr. Hepner: The optimal tax structure would include: a reformed corporate income tax, elimination of the franchise tax and many current tax preferences, reduction of state sales tax and increased reliance on deductible taxes such as income and property tax.

Dr. Campbell: The ideal system would be robust, transparent and difficult to alter and most importantly, would have the lowest possible transition costs. It would also provide government with sufficient revenue to perform its functions.

The fourth and final meeting of the Task Force was held on December 1, 2011… Presenters included three individuals who provided the Task Force members with the small business and practitioner perspective on tax reform. The Task Force heard from the following:

- Ron Barber, Barber & Bartz
- Bill Lohrey, Lohrey & Associates; and
- Jerrod Shouse, National Federation of Independent Business

1. Should the Oklahoma Constitution be amended to exempt all intangible personal property from the ad valorem tax?

Mr. Barber: Yes, because prior interpretations of the law have relied upon things such as goodwill being exempt and it would be unfair to change the interpretation now. Also valuation is tricky and would create uncertainty. Finally it might penalize the most innovative companies.

Mr. Lohrey: Yes, but this change should probably be phased in through a logical, slow method. For accounting purposes, it is important to know the rules at the beginning of each year.

Mr. Shouse: Yes, small businesses are particularly vulnerable to this tax.

2. Should Oklahoma tax business activity with a BAT, a corporate income tax, and a franchise tax as done under the present system or should one of those taxes be levied in place of the others?

Mr. Barber: Income tax should be the primary source and a properly implemented BAT tax could be a supplemental source. Taxes like the BAT and franchise tax are not the most sound and serve more as a backstop or floor to assure that businesses connected with the state pay something. There is a greater need to simplify the taxes than there is to lower them.

Mr. Lohrey: Income tax should be the primary focus. Simplicity and continuity are important for small business. Mr. Lohrey agrees with Mr. Barber and emphasizes that taxes like the BAT and franchise tax are more like “registration fees”.

Mr. Shouse: NFIB members are varied and the answer to this question might differ depending upon how they are structured. Anything that makes compliance simpler is better for small businesses.

3. Should Oklahoma enact stricter enforcement of taxes for online sales?

Mr. Barber: Yes, although this is a complex problem we must address it since such sales are only going to increase in the future. The best way to implement this is through cooperation with other states.

Mr. Lohrey: Yes, but this area is confusing so that is difficult to do.

Mr. Shouse: Yes, this is a fairness issue which affects brick and mortar businesses in Oklahoma.

4. *Should Oklahoma seek to reduce its income tax rate from its current level at5.25%? If so, what do you believe is the ideal income tax threshold?*

Mr. Barber: Yes, but if that results in a reduced level of services or shifting of the tax burden it will not entice anyone looking to move to or expand in our state. His client recently made a decision to expand an Oklahoma plant for a variety of reasons and tax structure was low on the list of reasons, especially when compared to quality of services available. A rate in the 4% to 5% range would probably be ideal if it is coupled with measures to maintain services.

Mr. Lohrey: It is not clear that the state is losing business because of the top rate so reducing it is not critical. If it is reduced, some rate between 4% and 5%, along with elimination of some credits, could be revenue-neutral.

Mr. Shouse: Yes, a reduction or elimination of income taxes would allow small businesses to invest more back into their operations. However, if the result is a shift to heavier reliance on sales tax, this would hurt small businesses.

5. How do you accomplish an income tax reduction and maintain revenue neutrality?

Mr. Barber: Revenue-neutrality could be accomplished by cutting expenses, eliminating certain tax credits, supplementing revenue decreases with changes in other tax types and reviewing the experience of other states to see if they have been successful in that way.

Mr. Lohrey: In Texas, the lack of income tax has resulted in a reliance on property taxes. That is no considered optimal. Continuing to look critically at tax credits and incentives is important as well as looking at the experience of other states.

Mr. Shouse: Although it is not clear how revenue-neutrality could be accomplished OCPA's plan is promising and Dank's Task Force is on the right track.

6. Should Oklahoma eliminate the income tax to be more competitive in a 21st century economy?

Mr. Barber: We should focus on other ways to improve our competitive position. If we determine that eliminating the income tax is necessary to be competitive, we must know the impact first and determine how states without income tax finance government services.

Mr. Lohrey: See answer to question #4.

Mr. Shouse: Although states without an income tax seem to be prospering, small business relies on state-provided services like education and transportation. This would be an important consideration.

7. If you could design your ideal tax system for Oklahoma, how would it be structured and why?

Mr. Barber: The income tax system could be modified by fixing the tax brackets, eliminating most, if not all, targeted credits, implementing some limits on deductions, possibly reducing rates if it will stimulate growth and adopting combined reporting for business. The Ad Valorem system could be improved by making a distinction in tax rates between residential and commercial properties and eliminating any tax on intangibles. For sales tax, groceries should be exempt and sales tax for online purchases should be fully collected. Oklahoma needs to retain its gross production tax. Finally, if a BAT tax is levied, it should be low and broad-based and the impact on groups like farmers and sole practitioners should be reviewed.

Mr. Lohrey: He agrees generally with Mr. Barber.

Mr. Shouse: Simplicity is greatly important because small businesses generally have less time and resources to devote to compliance.

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RECOMMENDATIONS AND CONCLUSIONS

Recommendation 1: The Task Force recommends that a constitutional amendment be put before the voters of Oklahoma to expand the scope of the existing constitutional ad valorem exemption for specified intangible property to cover any and all intangible property. The Task Force further recommends that the Legislature determine the most appropriate methodology for valuation of centrally assessed property.

Recommendation 2: The Task Force recommends that taxation of business activity in Oklahoma be simplified by allowing the business activity tax to expire on December 31, 2012 and by eliminating the levy of franchise tax completely. We anticipate that the $47 million in revenue collected for the franchise tax before the advent of the business activity tax will be offset by gains achieved under Recommendation 3.

Recommendation 3: The Task Force recommends that to minimize tax avoidance, corporations be required to use the accounting practice known as "combined reporting". The Task Force acknowledges, however, that the methodology for combined reporting varies from state to state therefore careful consideration should be given to the type of combined reporting requirements that best fit Oklahoma. It should be noted that combined reporting is required in 24 states, including the state of Texas.

Recommendation 4: The Task Force recommends that the corporate income tax rate be reduced from 6% to 5%. The revenue loss for this change is estimated to equal approximately $60 million. To offset the cost of the corporate rate reduction, we propose eliminating those tax credit items claimed by corporations which are targeted to narrow business interests. This includes provisions identified by the Task Force on Tax Credits and Economic Incentives, such as credits for: venture capital investments, coal production, rehabilitation of historic buildings, and energy efficient residential construction.

Recommendation 5: The Task Force recommends that the individual income tax rate be reduced in a revenue neutral manner. In agreement with individuals making presentations before the Task Force, we recommend that any change in the income tax rate must be coupled with the following:

- Thorough review of existing tax preferences with an expectation of reduction or elimination of most or all preferences;
- Recognition that in order to make Oklahoma attractive for business activity, the existing revenue stream flowing to core government services must be preserved and new revenue which may result must be used to fund priorities such as education and transportation; and
- Simplification of the tax structure.

Income tax rate: Reduce top marginal rate from 5.25% to 4.75%, in quarter-point increments over a two-year period.

Offset: [1] Eliminate the "value" of existing income tax preference items in Appendix A, over a two-year period by half each year (estimated revenue impact is + $352 million); and [2] Eliminate the advantage of the deduction for state and local taxes by requiring Oklahoma taxpayers who itemize deductions to "add back" such amounts on the state return (estimated revenue impact is + $67 million). Note: This deduction is already imbedded in the federal itemized deductions transferred to the Oklahoma income tax form.

Estimated net savings: $70.6 million (Based on revenue impact analysis by Oklahoma Tax Commission)

Recommendation 6: The Task Force believes that the adoption of Recommendation 5 will have a positive impact on overall revenue growth for the state of Oklahoma as income tax rates decline and the taxpayer base increases. Therefore, the Task Force recommends that the Legislature reinstate the income tax "trigger" provision in order to further reduce the top marginal rate by an additional quarter point, subject to growth in revenue. The reinstated provision would utilize 2011 fiscal year revenue amounts as a baseline for any future determinations rather than prior year amounts.

Recommendation 7: The Task Force recommends that if federal legislation such as the Main Street Fairness Act is enacted to address the issue of collection of the existing tax due on online sales, the estimated $180 million in additional sales tax revenue be used to reduce the top marginal income tax rate by a quarter point. The Task Force further recommends that the Legislature urge Oklahoma's congressional delegation to act to remove the competitive disadvantage that uncollected tax creates for Oklahoma's brick and mortar businesses.

Recommendation 8: Based on the assumption that Recommendations 1 through 7 become part of Oklahoma's tax structure, the Task Force recommends that the Governor and Legislature consider the long term goal of making Oklahoma a "no income tax" state. In order to reach that goal and create a significant economic competitive advantage for Oklahoma in a 21st Century service-driven economy, the following should be considered:

- Operating costs must be reduced where appropriate by making government more efficient;
- Core government services, such as education and transportation, which make Oklahoma attractive to business, must continue to be funded to the appropriate level;
- All tax preference items and incentive programs must be eliminated or reduced significantly;
- Sequentially lower income tax rates over a 7 to 10 year period must generate an increase in sales tax collections; and
- An intensive review must be made of Oklahoma's sales tax base as it compares to other states, particularly those which are "no income tax" states.

APPENDIX A

PROPOSED TAX PREFERENCE ITEMS TO ELIMINATE

Type	Citation	Estimated revenue impact
Investment in Equipment Used for Recycling, Reuse, or Source Reduction of Hazardous Waste	27A O.S. §2-11-303	$3,300
Child Care	68 O.S. §2357	$28,991,000
Gas Used in Manufacturing	68 O.S. §2357	$79,000
Oklahoma Investment/New Jobs	68 O.S. §2357.4	$28,497,000
Energy Conservation Assistance Fund	68 O.S. §2357.6	$21,000
Venture Capital	68 O.S. §2357.7	$12,294,000
Oklahoma Coal Production	68 O.S. §2357.11	$4,276,000
Agricultural Processing Facilities	68 O.S. §2357.25	$2,517,000
Child Care Services- Employers	68 O.S. §2357.26	$33,000
Child Care Service Providers	68 O.S. §2357.27	$198,000
Coast to Coast Airline Service	68 O.S. §2357.28	$2,000
Ad Valorem Tax (Tornado)	68 O.S. §2357.29	$26,000
Small Business Guaranty Fee	68 O.S. §2357.30	$227,000
Credit for Electricity Generated by Zero-Emission Facilities (Wind power generation)	68 O.S. §2357.32A	$1,239,000
Credit Manufacturers of Advanced Small Wind Turbines	68 O.S. §2357.32B	$775,000
Hepatitis Immunization	68 O.S. §2357.33	$19,000
Tax Credit for Qualified Rehabilitation Expenditures (Historic Buildings)	68 O.S. §2357.41	$671,000
Oklahoma Earned Income Tax Credit	68 O.S. §2357.43	$31,887,000
Donations to Biomedical Research Foundations or Cancer Research Institutes	68 O.S. §2357.45	$364,000
Energy Efficient Residential Construction	68 O.S. §2357.46	$3,776,000
Modification expenses paid for an injured employee	68 O.S. §2357.47	$33,500
Qualified Recycling Facility	68 O.S. §2357.59	$32,000
Investment in Qualified Small Business Capital Companies	68 O.S. §2357.62	
Investment In Small Business Ventures	68 O.S. §2357.63	$11,060,000
Investment in Rural Venture Capital Companies	68 O.S. §2357.73	
Investment in Rural Small Business Ventures	68 O.S. §2357.74	$37,406,000
Local Development and Enterprise Zone Investment Incentive Credit	68 O.S. §2357.81	$150
Poultry Litter Tax Credit	68 O.S. §2357.100	$173,000
Film and Music Profit Reinvestment Credit	68 O.S. §2357.101	$34,000
Dry Fire Hydrant Credit	68 O.S. §2357.102	$45,000
Railroad Modernization Credit	68 O.S. §2357.104	$1,130,000
Specially Trained Canine Credit	68 O.S. §2357.203	$129,000
Blind Individuals	68 O.S. §2358	$130,722

Type	Citation	Estimated reven impact
Individuals Sixty-five (65) or older	68 O.S. § 2358	$474,30
Taxpayers with Physical Disabilities	68 O.S. § 2358	$42,68
Dividend/Interest Income Exclusion	68 O.S. § 2358	$1,691,28
Nonrecurring Adoption Expenses	68 O.S. § 2358	$155,26
Oklahoma College Savings Program	68 O.S. § 2358	$2,412,12
Political Contributions	68 O.S. § 2358.3	$138,75
Volunteer Firefighter Credit	68 O.S. § 2358.7	$418,00
Loans by Financial Institutions under Rural Economic Development Loan Act	68 O.S. § 2370	$35,00
Stafford Loan Origination Fee	68 O.S. § 2370.3	$349,00
Low Income Property Tax Relief	68 O.S. § 2908	$226,00
Film Enhancement Rebate	68 O.S. § 3624	$5,000,00
Sales Tax Relief	68 O.S. § 5011	$43,212,00
Research and Development Incentives Act	68 O.S. § 54006	$14,00
TOTAL		**$352,936,27**

notes:

1. This list includes only those income tax preferences for which a revenue impact was reported Commission for the most recent data period in the TAX EXPENDITURE REPORT. It does not inc zero amount or those where data was not available.

2. The timing of any "savings" realized would be delayed due to the difference in the calendar an

3. Some of the amounts have been updated by the OTC and differ from the most recent Tax Expe

4. Because some tax credits are eligible to be carried over for anywhere from 3 to 20 years, cre earned could continue to be claimed for a period of time after the credit itself is eliminated.

5. Certain preferences have been subject to sunset recently or are scheduled to sunset within th This means the revenue impact shown here may be inaccurate in future years.