Maryland in disequilibrium

Bringing the state's tax structure more in line with our neighbors may help Maryland appear more business friendly

December 29, 2013 | By Anirban Basu and Zach Fritz

How did it come to this? Between 2007 and 2012, the State of Maryland raised taxes and fees 24 times according to Change Maryland, including raising income taxes during a 2012 special legislative session, increasing the sales tax on alcoholic beverages from 6 percent to 9 percent in 2011, and levying a hospital assessment that year. Despite these revenue enhancements, the state faces unexpectedly large fiscal deficits this year and next. What was estimated to be a $300 million surplus for fiscal year 2014 is now an $87 million deficit. The gap for fiscal 2015 is estimated at roughly $400 million, according to Maryland's Department of Legislative Services.

Given anticipated improvements in national economic activity built into state budgetary forecasts, Maryland must be in disequilibrium. Our economy is simply not expanding quickly enough to finance all of the spending in which Annapolis' policymakers collectively want to engage.

Among the more problematic aspects of Maryland's fiscal structure are repeated shortfalls in corporate tax revenues. In March 2013, the Board of Revenue Estimates projected that corporate income tax revenues would come in at $822.6 million for fiscal 2014. By September, the forecast had been revised downward to $755.5 million, a difference of $67.1 million. The revised fiscal 2014 estimate is actually less than realized corporate income tax revenues for fiscal 2013. Given continued improvement in global and national corporate performance, these dynamics are alarming.

They also serve to spotlight Maryland's fundamental economic problem — an economy too dependent upon government and insufficiently attractive to private enterprise. Maryland has much about which to boast — highly-ranked public schools, the Port of Baltimore, an incredible network of highways, tourist destinations, BWI and elevated concentrations of scientists, engineers, financial professionals, health-care workers and university professors.

We should be Singapore. Instead, we are increasingly poor and not nearly the most competitive economy in our region. The Census Bureau estimates that nearly one in 10 Marylanders lived below the federal poverty threshold between 2008 and 2012, translating into nearly 550,000 people.

Policymakers in Annapolis might conclude that what we need is more spending and social assistance. Perhaps, but what we really need is a lot more jobs. This is where our lack of business climate competitiveness really hurts. Many will remember the decision by Northrop Grumman to choose Virginia over Maryland for its global headquarters in 2010. In 2012, contracting giant Bechtel relocated 625 employees and $18.5 million in investment from Frederick to Reston. Other corporations that have selected Virginia over Maryland include Hilton Worldwide, Computer Sciences Corporation, SAIC and Volkswagen North America.

One rarely hears of major private employers moving in the other direction. Why? It's certainly not because we care less about our families, suffer worse traffic or are less educated. In fact, we are competitive with the Commonwealth of Virginia along most dimensions.

One exception — taxes. Maryland's lofty tax rates, including its high corporate and personal income taxes working in conjunction with our willingness to tax both estates and inheritances, appear to be driving both business and residents away, including into southern Pennsylvania. As an aside, our out-migration enhancing tax policies don't square particularly well with the State of Maryland's anti-sprawl mantra.

A recent study by the non-partisan Tax Foundation shows just how serious the out-migration of taxpayers has become. From 2000 to 2010, 66,000 residents along with $5.5 billion in taxable income left the state on net. Among the states to which Marylanders fled in large numbers were Virginia, North Carolina and Pennsylvania. Granted, people may leave a place for many reasons, including in search of warmer weather. However, that does not explain why Virginia, with its similar climate, experienced net in-migration of taxable income.

Maryland's recent fiscal disappointments are largely due to the fact that businesses and people are mobile. If raising tax rates produced no countervailing impacts, tax revenues would rise in predictable fashion. But the fact is that in a world in which businesses are striving to maximize profits and where households are trying to hold on to earnings, raising taxes and fees generates economic responses —responses that have translated into massive fiscal disappointment.

Bringing Maryland's tax structure more in line with our neighbors may produce some positive fiscal surprises by keeping more businesses and residents here.

Anirban Basu and Zach Fritz are analysts with the Sage Policy Group, Inc. Their respective emails are abasu@sagepolicy.com and zfritz@sagepolicy.com.

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