SIMPLIFYING & CUTTING OKLAHOMA'S INCOME TAX WITHOUT BLOWING UP THE BUDGET

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Income taxes inhibit capital investment, the juice that makes the engine of the economy hum. Full elimination of the personal income tax may be lawmakers' ultimate goal, but getting there while adequately funding state government will take time. That doesn't mean the state should wait to get started on pro-growth tax reform. As the saying goes, the best time to plant a tree is yesterday.

SCRF's income tax proposal does 3 things:
- **Cuts taxes** immediately;
- **Simplifies** taxpayer compliance; and
- Phases-in future tax cuts in a **fiscally responsible** manner.

1. CUT THE RATE FROM 4.75% TO 4.25%

With record state revenue collections for several years running, state government can absorb a **modest tax cut of .5%** without seeking offsetting new revenue. For perspective, the estimated fiscal impact to the state of a half-point income tax reduction with no other changes to the income tax is $182.2 million.[1] This figure represents **less than 1.5% of Oklahoma's $12.7 billion state budget**. If this initial tax cut truly reduces tax collections by the amount projected—always an open question with estimates that do not factor in economic growth spurred by the cut—Oklahoma state government would still be left with a larger budget than any year in its 117-year history. For Oklahoma taxpayers going on a third year facing down record inflation, however, this immediate tax cut would provide meaningful relief.

2. MOVE TO A SINGLE-BRACKET FLAT TAX WITH A HIGHER STANDARD DEDUCTION

Oklahoma should eliminate its unnecessarily complicated six (6) income tax brackets and replace them with a Single Bracket Flat Tax. The flat tax rate would be set at the post-cut rate of 4.25% in the first year, with a nearly doubled standard deduction of $10,350 for individuals and $20,700 for joint filers (up from $6,350 and $12,700 respectively). By raising the standard deduction while eliminating the lower-income brackets, lawmakers would ensure tax relief for all taxpayers, not just those at the top.

3. RESPONSIBLY PHASE-IN FUTURE TAX CUTS TO GET TO 2.75%

As Oklahoma simplifies its income tax to a single bracket, lawmakers should put in place a mechanism that ensures continued downward pressure on the rate as Oklahoma's economy (and state revenue) grows. Revenue triggers will keep momentum for future tax relief and send an important signal to businesses and individuals that the future trajectory of the state is toward a maximally competitive tax environment. If designed correctly, these planned rate reductions will, by definition, avoid revenue disruptions because they will be made contingent on growing tax collections.

Specifically, our proposal calls for phased-in half-point tax cuts to be triggered when state government revenue collections meet or exceed target growth benchmarks. The new flat income tax rate would be reduced by .5% each year if state revenue collections exceed 1.5% annual revenue growth over the benchmark year. After three years of sufficient revenue growth, the state would reach a final rate of 2.75%, making Oklahoma extremely competitive nationally. Importantly, revenue triggers should be pegged to December Certified Collections (the amount actually collected by the state), not February Estimates of what the state anticipates it will take in. This approach ensures that numbers cannot be manipulated to either force a tax cut that should not take place or prevent one that should.

1 HB 1954, filed during the 2023 regular legislative session, would have implemented this proposed cut. The Revenue Impact Statement produced by the Oklahoma Tax Commission using microsimulation estimated a decrease of $182.2 million in income tax collections.

FISCAL IMPACT

-To get to the initial **4.25% rate**, the state would forego an estimated **$182.2 million** in revenue. This would keep overall state revenue at roughly the same level it was in FY2023, hardly a difficult budget year.

- Moving to a **single bracket flat tax** while simultaneously raising the standard deduction is designed to be a **revenue neutral** move. That is, the standard deduction is raised to offset the effect of subjecting lower income levels to the new higher single rate, but is not raised beyond the level necessary to avoid a tax increase on lower incomes. This approach simplifies compliance for taxpayers, but does not give up revenue to the state.

- **Future rate cuts based on revenue triggers** will cause the state to forego revenue that would be collected were the cuts not made, but will be taken from revenue growth. If structured as proposed in this plan, these cuts **will not have a direct fiscal impact on current government operations**, which will continue to grow by at least 1.5% per year.

PRO-GROWTH INCOME TAX REFORM FOR OKLAHOMA

SCRF's income tax proposal will provide immediate tax relief to individuals and families while stimulating investment and growth in Oklahoma's economy. The plan achieves these objectives in a fiscally responsible manner, protecting the state's ability to meet its needs without significant revenue disruptions.

- Incentivizes Work. A flat rate does not disincentive work like a progressive income tax does. A graduated income tax punishes work and success since the more an individual makes, the higher their tax rate will become. Disincentivizing work stunts economic growth.

- Encourages Fairness. A flat rate income tax prevents the singling out of one particular group of earners and raising, or cutting, their taxes.

- Simplifies Compliance. Progressive income taxes require a tax table and unnecessarily complicated calculations for taxpayers to determine what they owe. A flat rate income tax is simple to comply with and administer.

- Avoids Budget Problems. By cutting rates in phases over time and only when state revenue growth is sufficient, the state can ensure budget stability and predictability.