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BUDGET & TAX CENTER

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Lowering the income tax cap in the state constitution is a bad deal for North Carolinians

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The NC General Assembly has passed a bill to put a constitutional amendment on the ballot in November that, if approved by voters, would lower the maximum allowable income tax rate to 3.5 percent. The state constitution already limits the maximum income tax rate, but this new, even lower income tax cap would lock in tax breaks for the wealthy and profitable corporations.

- It would block future lawmakers from choosing fair revenue options when needed.
- It would have no immediate effect on how much people are paying in taxes, because the personal income tax rate will already go to 3.49 percent in 2027.
- The corporate income tax rate is already at 2 percent and will be completely eliminated by 2030 unless legislators reverse course.

NC is faced with rising costs, and North Carolinians want their elected leaders to fund the things that will make their life more affordable like child care, affordable housing, and health care. They also want investments that connect their families and neighbors to opportunity through excellent public schools, affordable public universities and community colleges.

A 3.5% INCOME TAX CAP IN OUR STATE CONSTITUTION WOULD:

Further lock NC into an upside-down tax code that benefits the super-rich and highly profitable corporations

When it comes to state and local taxes, North Carolina already has an upside-down tax code that asks the most from families with the least. The richest 1 percent of households in our state make well over $1 million each year on average but pay just 6 percent of their annual income in state and local taxes. Meanwhile, the average household in the bottom 20 percent, making less than $22,000, still pays 11 percent in taxes — a portion almost twice as high as the millionaires.

This amendment would lock in a 3.5 percent cap on personal and corporate income taxes, blocking lawmakers from restoring a more equitable tax code that asks wealthy people to pay a higher rate. Cutting corporate income taxes is a bad deal for North Carolina because more than 90 percent of the tax benefits go to people outside the state, primarily corporate shareholders and wealthy executives.

Stricter limits on income taxes also mean a greater reliance on more regressive revenue sources like sales taxes, fines, and fees. People with lower incomes spend a far greater share of their earnings on purchases subject to sales tax than wealthy people, and these taxes are already a growing share of state revenue. A lower income tax cap will lock in these bad choices.

A 3.5% INCOME TAX LIMIT IN OUR STATE CONSTITUTION WOULD:

Make it harder for our state to provide adequate public services and jeopardize our credit rating

By lowering the income tax cap from 7 percent to 3.5 percent, this amendment would block our state from generating $17 billion in annual public revenue from personal and corporate income taxes— an amount that will grow over time. North Carolina families are already seeing the impacts of keeping taxes low for the wealthy few and profitable corporations: tuition increases across the UNC system, teachers leaving our public schools for higher-paid positions in Virginia, record closures of child care programs, and more. With an adequate and fair tax code, our state could address these issues and make life easier for us all, but a 3.5 percent income tax cap would make that all but impossible.

When income tax limits are put into the state constitution, they can also damage a state's credit rating, making it more expensive for governments to borrow money for infrastructure and similar projects. **Major credit rating agencies in the U.S. name constitutional limits on taxes as a negative factor for bond ratings because they severely constrain government's options for repaying loans.** Not surprisingly, research has found that more restrictive state tax limits are associated with lower credit ratings and higher borrowing costs.

Tie lawmakers' hands in the future and prevent them from being accountable to their constituents

If the income tax cap in our state constitution is lowered, it will be extremely difficult to undo. During recession in the 2000s, North Carolina lawmakers were able to temporarily raise income taxes on people with very high incomes, taking pressure off local governments and generating millions of dollars in funding to support public schools facing budget shortfalls. **Research has shown that if the goal is long-term economic health, raising taxes on people with high incomes is a better strategy than spending cuts during a recession.**

A lower tax cap would tie lawmakers' hands, limiting their tools to respond to their constituents' needs with public funds generated through tax policies that ask the wealthy and profitable corporations to pay their fair share. At a time when the state is faced with rising costs from federal cuts to health care and food assistance, and current funding levels are leaving needs unmet, a lower cap would also hamstring future elected leaders' ability to make different policy decisions than the bad ones being made today.

Increase pressure on local governments — especially rural counties — while the property tax amendment could limit local options

State revenue is an important source of funds for many counties and cities, so a state income tax cap will have ripple effects on local services. **At least one-third of NC counties, which are overwhelmingly rural, rely on state funds for over 15 percent of their annual budget. These counties will be hit the hardest when state legislators can't adjust income tax policy to meet funding needs.** Facing limited state support, local governments will have even fewer choices if legislators also pass property tax limits.

For citations and sources, go to NCBudget.org/TaxCap