Better Choices For CT

Revenue Options

February 2010

Finding Needed Revenue

Delay Reductions in the Gift and Estate Tax - $75 million over the biennium

The continuing revenue shortfall has prompted a delay in a planned reduction in the sales tax. If we cannot afford an across-the-board tax reduction, surely we cannot implement estate tax cuts that would exclusively benefit Connecticut's wealthiest individuals. Delaying the estate tax reduction will preserve a vital revenue stream and promote fairness.

Make the Personal Income Tax More Progressive – up to $600 million/year

Even after Connecticut's recent income tax increase for very high-income households, Connecticut's wealthiest families still pay a much lower share of their income in state and local taxes (4.9%) that middle-income families (9.9%) and low-income families (12.0%). Adopting income tax rates of 6% on couples' income over $200,000, 7% on couples' income over $500,000, and 8% on couples' income over $1 million would make our overall tax structure more balanced and preserve funding for crucial publicly funded programs. (The recently passed Oregon tax referendum raises rates to 10.8% on income over $250,000 and to 11% on income over $500,000.)

Increase Sales Tax Revenue and Equalize Contributions - $210 million/year

The sales tax is an important revenue generator but one that asks more from lower-income taxpayers than from higher-income residents. A half-percent increase in the sales tax (to 6.5%) would raise about $260 million a year and still leave Connecticut's rate below neighbors such as Rhode Island (7%), New York City (8.25%), and New Jersey (7%).

To correct for the disproportionate burden the sales tax places on working- and middle-class families, the state should adopt a refundable **Earned Income Tax or Sales Tax Credit** targeted to middle- and low-income families at a cost of about $50 million a year.

Alternatively, we could raise a similar amount of revenue without raising the rate by modernizing the state sales tax and applying the 6% tax rate to services in the same way that we apply it to goods. Rather than specifying which services are taxed, services should be taxed unless they are explicitly exempted by statute.

Restore the Scheduled Petroleum Gross Earnings Tax Rate Increase - $20-25 million/year

As gas prices soared in 2008, Connecticut eliminated a scheduled 0.5% increase in the Petroleum Gross Earnings Tax (from 7.0% to 7.5%). Since the rate reduction was enacted, crude oil prices have fallen nearly 40% and retail gasoline prices have fallen more than 30%. Since prices have plummeted, it is time to restore this scheduled rate increase. When the increase was halted, the Office of Fiscal Analysis estimated that Connecticut would lose $30.8 million in General Fund revenue and $3.9 million in Transportation Fund revenue per year between FY 09 and FY 13. Given that petroleum prices have fallen, a restoration of the scheduled increase is expected to generate somewhat less revenue.

Raise Taxes on Unhealthy Products – more than $15 million a year

Raising taxes on items with negative health consequences can raise revenue and encourage healthy behavior. Taxes on cigarettes were raised last year; this year we should consider increases in taxes on alcohol, soft drinks, and fast foods. According to the tax calculator designed by the Rudd Center for Food Policy and Obesity at Yale University, a tax of 1 cent on every 12 ounces of soda consumed in Connecticut would raise more than $15 million a year.

Transparency, Accountability, and Fairness

Evaluate and Reduce Unwarranted Tax Expenditures

Connecticut's state tax code contains about $5 billion dollars in credits, deductions, rate reductions, and exemptions that favor some business and individual activities over others and also diminish state revenue. Yet there is no system to evaluate whether these tax expenditures are an efficient use of resources and no way for the public to know who benefits from these tax reductions. The General Assembly has embraced the principles of Results-Based Accountability (RBA) in evaluating direct appropriations. Tax expenditures merit equally rigorous review.

Adopt Mandatory Combined Reporting to Close Corporate Income Tax Loopholes

Connecticut's tax system allows large, multi-state corporations to shift profits to subsidiaries in states without corporate income taxes. This enables larger corporations to avoid their fair share of taxes, costing the state millions of dollars and shifting tax responsibility onto local businesses and individuals. Twenty-three states have already adopted mandatory combined reporting.

Review and Restructure Business Taxes

Business taxes in Connecticut have not been comprehensively evaluated since the early 1990s using principles of good government such as fairness, accountability, and cohesion. Connecticut's business taxes must be restructured to adequately support the public structures that enable a healthy business environment. Connecticut should convene a Business Tax Commission—similar to the commission recently convened in Massachusetts—to recommend changes to our business tax structure and ensure that these taxes bear a fairer relationship to a company's profitability and footprint in the state.

Position the State to Tax Internet Sales

The inability of states to enforce taxation of sales over the Internet lowers state revenues and puts local businesses at an unfair competitive disadvantage. Connecticut should modernize the sales tax by positioning itself to effectively tax internet sales as these issues are addressed at the federal level and through interstate compacts.