

**Testimony Regarding
House Bill 6560: An Act Concerning Disclosure of Tax Incentives Provided to
Business**

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Committee on Finance, Revenue and Bonding
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Senator Daily, Representative Widlitz and members of the Finance Committee:

I am testifying today on behalf of Connecticut Voices for Children, an independent child advocacy organization that serves as a member of the State Fiscal Analysis Initiative, a nationwide network of organizations that advocate for responsible state fiscal policy with a particular focus on the needs of middle- and lower-income families. I am a Senior Policy Fellow at Connecticut Voices, concentrating on state fiscal policy.

Today I submit testimony **in support** of House Bill 6560 for the following reasons:

- Tax expenditures have been quickly eroding Connecticut's corporate and insurance premiums tax base. The amount of revenue that Connecticut collects through the corporate income tax, for example, has declined to such a low level that recently Connecticut ranked the **fifth lowest** in total state and local business tax revenues among states when compared to the level of private sector economic activity in each state.¹
- However, for many of these expenditures there is no public disclosure of who receives them, in what denomination, or for what specific purpose.
- Transparency in business tax credits, deductions, and exemptions, such as would be promoted in HB6560, is needed to assure greater accountability for the economic return of these investments.
- Moreover, Connecticut needs to move towards a system where all economic development efforts through both the appropriations and revenues side are reported and evaluated against Connecticut's long-term development goals, such as in a "unified development budget," which would report, on a company and project specific basis, the total in public subsidies provided toward economic development.

Why business tax subsidies matter. Business tax credits, deductions and exemptions are a form of government spending: they often result in a net loss of Connecticut state revenue and, since the state budget must be balanced, must be offset by cutting funding for other programs or services or by raising taxes on other taxpayers. Consider tax credits: Connecticut has spent **hundreds of millions of dollars** in recent years awarding tax credits to a small fraction of the corporations that do business in the state.² The total amount of state revenue spent through business credits has also been on the rise, increasing 20-fold between 1987 and 2007.³ At the same time, Connecticut faces a budget crisis that is unprecedented in scope, and threatens the state's economic vitality and quality of life. **In his budget, the Governor has proposed several cuts that will severely hamper or**

eliminate public programs that protect children or that shift costs currently borne by the state onto low-income families.⁴ The negative impact of such proposals should be weighed against the benefits, if any, of this growing assortment of preferential tax breaks some corporations receive. However, there is currently no comprehensive or independent system by which to determine the value or effectiveness of tax credits or other tax expenditures, even as they continue to grow unchecked. In the painful process of bringing our fiscal house in order, Connecticut simply cannot afford to leave hundreds of millions of dollars in questionable spending unexamined.

More transparency of business subsidies will better enable citizens and lawmakers to impose standards of accountability, and set priorities. Unlike economic development assistance awarded through the Department of Economic and Community Development (DECD), which creates a paper trail regarding the economic benefits awarded to a corporation, the corporation benefiting, the expected benefits to the state from the award and the like, there is no comparable oversight for tax expenditures. There also is no inquiry into the opportunity cost of our current expenditures through the tax code. For example, if the hundreds of millions in tax credits were invested into *different* industries or projects, could Connecticut get even greater economic return? If the credits were repealed and the additional revenue then collected invested in other forms of economic development, might there be greater return on our investment? **Many of these questions cannot even start to be answered if we don't know which businesses benefit—and by how much—from the credits, deductions, and exemptions that Connecticut awards them. HB6560 would require this minimum standard of transparency.**

Furthermore, tax expenditures are not subject to the same standards of transparency and accountability as direct economic aid. Unlike appropriated spending that is reviewed and reauthorized *each year* and – increasingly – is subject to a Results-Based Accountability (RBA) process, tax expenditures are *not* reviewed annually. Once enacted into law, tax expenditures become, and remain, “entitlements.” There is no further regular inquiry by the General Assembly as to whether they are continuing to fill an important public purpose (e.g. creating new jobs). Notably, even the Corporation Business Tax Credit Review Committee – established to help provide oversight -- has failed to meet regularly, study the existing credits, and submit its recommendations, as is required by state law.⁵

Many existing subsidies are ineffective, and some may be damaging to Connecticut's economy. In 2005, Connecticut's Finance, Revenue and Bonding Committee asked the University of Connecticut Center of Economic Analysis (CCEA) to evaluate the impact of the state's corporate tax policy. The ensuing report showed that 14 of the 24 studied corporate tax credit programs in Connecticut led to net job *losses*. Indeed, one of Connecticut's largest tax credits, the fixed capital investment credit, added 333 private sector jobs but reduced public employment by 559 jobs, for a net loss of 226 jobs.⁶ Additionally, the Program Review and Investigation Committee's 2005 study of Connecticut's Tax System concluded that, “[b]ased on usage alone (not considering other measure of effectiveness)” sixteen of the twenty-six business tax credits that then existed “appear of little benefit to the state's economy, and should be eliminated.”⁷ A number of these credits were established under the rationale of creating incentives for certain business activities

but are rarely claimed, providing some evidence of the credits' ineffectiveness.⁸ More recently, Connecticut's own Department of Economic and Community Development, which administers several of the state's business tax credit programs, also reported serious flaws in the programs, to little legislative effect.⁹ Clearly, tax credits that are inefficient, ineffective, or damaging should be repealed, yet several credits persist unchallenged despite evidence that question their usefulness.

Connecticut should move toward a system where *all* state economic development programs are evaluated together according to a long-term economic plan. Today, Connecticut funds economic development efforts through a patchwork of grants, loans, and tax expenditures, administered across several governmental and quasi-governmental agencies. This collection of development efforts is disorganized, largely opaque, and not subject to any process of oversight to ensure that they are coordinated and mutually supportive of one another.

A "unified development budget" would report in a single document, by firm individually and by industry in the aggregate, all economic development assistance, no matter what the form. Connecticut could require that OFA publish a biannual Unified Development Budget Report that includes all state on-budget and off-budget economic development spending through grants and loans by public and quasi-public agencies, as well as through preferential tax breaks. The Report could: a) include tax expenditures and major tax code changes designed to enhance economic development; b) categorize (by type of benefit, purpose of benefit, and type of beneficiary) total state spending on economic development; c) include all state spending to foster job creation, technology development, a healthy business sector, and help for employers in securing a skilled workforce, whether the spending is through grants, loans, tax expenditures or other preferential tax code changes; and d) include all on-budget and off-budget economic development spending through state agencies and through quasi-public agencies for the benefit of for-profit and not-for-profit entities. To assure that the data in the Report are complete, the state would require annual incentive-specific reporting for each economic development investment—Increased disclosure from the Department of Revenue Services, such as would be required in HB6560, would be instrumental towards this purpose.

As the state economy continues to falter, and business tax expenditures quietly but increasingly erode state revenues, the need to assure greater accountability for the economic return of these investments becomes ever more essential. **As Connecticut confronts its largest state budget deficit in history, *all* forms of spending, including economic development efforts using tax credits, deductions, and exemptions, must be reviewed critically and comprehensively.**

¹ Quantitative Economics and Statistics Practice of Earnst & Young, "Total State and Local Business Taxes: State-by-State Estimates for Fiscal Year 2009." March, 2010. [http://www.ey.com/Publication/vwLUAssets/Total-state-and-local-business-taxes-March-2010/\\$FILE/Total-state-and-local-business-taxes-March-2010.pdf](http://www.ey.com/Publication/vwLUAssets/Total-state-and-local-business-taxes-March-2010/$FILE/Total-state-and-local-business-taxes-March-2010.pdf)

² According to the Department of Revenue Services, Connecticut has spent over \$100 million per year on corporate tax credits since 1997. In 2007, \$110 million in credits were claimed against the corporate income tax and an addition \$75 million were claimed against the Insurance Premiums Tax. Connecticut Department of Revenue Services. Financial Year 2008-2009 Annual Report. p. 35. http://www.ct.gov/drs/lib/drs/research/annualreport/drs_fy09_annual_report.pdf;

Insurance Premiums Tax data in: Department of Revenue Services. Financial Year 2007-2008 Annual Report. p. 40.
http://www.ct.gov/drs/lib/drs/research/annualreport/drs_fy08_annual_report.pdf

³ Joachim Hero and Shelley Geballe, "Time for Connecticut to Reexamine its Business Tax Credits." Connecticut Voices for Children. April, 2010.

⁴ Some proposed cuts include: Charging some children and most adults co-payments for preventive care and other services of up to 5% of family income annually; the elimination of 7 out of 9 positions within the Office of the Child Advocate (OCA), the "watchdog" agency with statutory authority to provide independent oversight and monitoring of the care and protection of the state's children; limiting or removing inflation-related increases in foster care and adoption subsidies and residential payments; and the elimination of a newly created \$1 million program to support homeless youth.

⁵ Conn. Gen. Stat. §12-217z.

⁶ William F. Lott and Stan McMillen. *The Economic Impact of Connecticut's Corporate Tax Policy Changes: 1995-2012*. Connecticut Center for Economic Analysis. December 8, 2005. Pg. 18.

⁷ It found that ten of the twenty-six credits were used by five or fewer filers, and six of the twenty-six each account for \$5,000 or less in credit value. Legislative Program Review and Investigations Committee, *Connecticut's Tax System* (2006), p. 203.

⁸ There are several Connecticut credits that were established under the rationale of providing business incentives that have not been amended in ten years or more and were not claimed at all during 2007 (the most recent year for which we have claims data): the displaced electric worker credit, the manufacturing service facility credit, the financial institutions credit, and the enterprise zone credit.

⁹ DECD has repeatedly raised concerns, for example, about the structure of the insurance reinvestment credit, which provides tax credits to managers of funds in Connecticut that invest in insurance businesses. It found that the cost of the credit per job ranged from \$173,418 to \$1.13 million and recently stated of the credit that, "the cost versus benefit to the state has not met the original intent of the legislation." Department of Economic and Community Development, *Annual Report for Fiscal Year 2008-2009*. February 1, 2010. p. 280. PA 10-75 has amended the credit and created new provisions that would provide a 100% tax credit against the insurance premiums tax to approved fund managers that provide financing to eligible businesses, such as those that are 25% committed to "green technology."