CONNECTICUT VOICES FOR CHILDREN

20 YEARS OF ADVANCING OPPORTUNITIES FOR CHILDREN AND FAMILIES

Testimony Supporting H.B. 5636: An Act Concerning Municipal Taxing Districts, the Sales Tax, the Apprenticeship Tax Credit, Certain Fees and the Tax Credit Report

Nick Defiesta
Finance, Revenue and Bonding Committee
March 22, 2015

Senator Fonfara, Representative Berger, and distinguished members of the Committee:

I am Nick Defiesta and I am testifying today on behalf of Connecticut Voices for Children, a research-based public education and advocacy organization that works statewide to promote the well-being of Connecticut's children, youth, and families.

We are testifying in support of H.B. 5636, particularly the provision that expands the Tax Credit Report. We also respectfully urge the Committee to expand the Tax Expenditure Report in a similar manner to the changes to the Tax Credit Report in this bill.

H.B. 5636 requires the Department of Economic and Community Development to expand the Tax Credit Report by more fully evaluating the effectiveness of tax credits "enacted for the recruitment or retention of businesses." This evaluation includes a description of the tax credit, its beneficiaries and its goals; an analysis of its fiscal and economic impact alongside administrative costs; and a recommendation as to whether to continue, modify, or repeal each tax credit. The bill also requires this Committee to hold a public hearing on the report.

According to Good Jobs First Subsidy Tracker[1], which records the level of tax incentives provided to businesses for economic development, Connecticut awarded $710.0 million in tax incentives in 2014, the latest year for which full data is available. A Good Jobs First report found that the majority of these incentives – between 80 and 96 cents on the dollar – go to big businesses.[2] H.B. 5636 will provide regular evaluation of this spending to ensure its intended goals are being met.

These changes will provide accountability and transparency to a part of our tax code that too often goes unexamined. During a time of fiscal austerity, it is incumbent that the state analyze all types of spending, including spending through tax credits, to ensure all spending is meeting its goals in a cost-effective manner. If such tax credit programs are evaluated to be operating efficiently, they should be continued or expanded; if they are found to be an ineffective use of scarce taxpayer resources, they should be ended. The Tax Credit Report provision in this bill would bring the state closer to this goal.

We respectfully urge the Committee to apply the same logic more broadly to all tax expenditures, which are estimated to cost the state over $6.4 billion in revenue in the coming fiscal year. The tax incentives to be evaluated in the Tax Credit Report are only a subset of what are known as tax expenditures, which include exemptions in the sales tax, lower rates for

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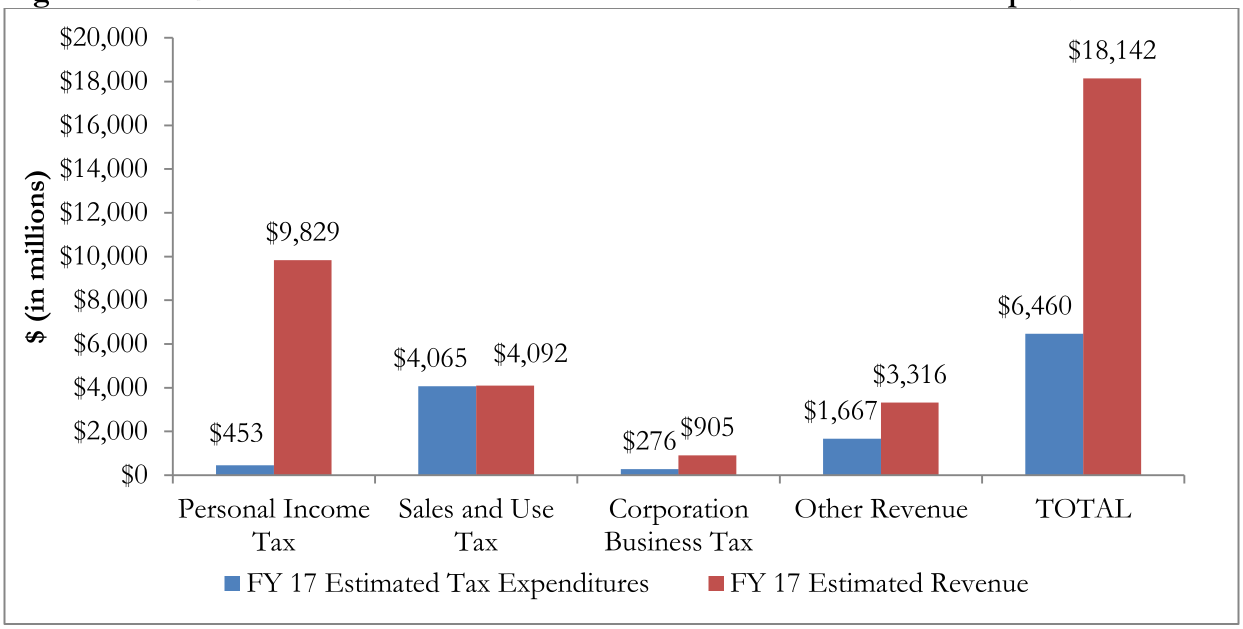
[1] Accessible at: http://www.goodjobsfirst.org/subsidy-tracker

[2] LeRoy, Greg *et al.* "Shortchanging Small Business," Good Jobs First, October 2015. Accessible at: http://www.goodjobsfirst.org/sites/default/files/docs/pdf/shortchanging.pdf

certain corporations[3], and personal income tax deductions. Tax expenditures, like tax incentives, are akin to spending in that they cost the state money it would otherwise collect, lead to higher taxation or lower spending elsewhere in the budget, and can be used to achieve policy objectives.

Despite these similarities, tax expenditures are not subject to the appropriations process that dictates – each and every year — precisely how state funds will be spent. Thus, tax expenditures – which in the coming fiscal year are estimated to amount to over $6.4 billion – persist year after year with *minimal* review as to whether they are addressing critical state needs in a cost-effective way. Figure 1 shows the scale of the revenue lost to tax expenditures compared to the revenue estimated for FY 17.

Figure 1: FY 17 Estimated Revenue Collection vs. Revenue Lost to Tax Expenditures



Sources: Office of Fiscal Analysis 2016 Tax Expenditure Report, Governor's FY 17 Midterm Budget Proposal. "Other Revenue" includes the Cigarette Tax, Motor Fuels Tax, Health Provider Tax, and all other revenue sources.

If the Committee seeks to evaluate whether tax incentives are achieving their policy objectives in a fiscally responsible manner, then this same logic should be applied to tax expenditures. At present, tax expenditures are listed in a biennial report by the Office of Fiscal Analysis (OFA) that is similar to the Tax Credit Report expanded by this bill. In the "Connecticut Tax Expenditure Report,"[4] OFA describes each tax expenditure, the year it was enacted, its purpose, the estimated amount of revenue that would be gained if the expenditure were repealed, and the number of taxpayers benefitting. While the report provides useful detail, it does not offer *evaluation* – that is, an appraisal of how well the tax expenditures are functioning, the extent to which they are meeting their policy goals, and ultimately, whether each tax expenditure should be continued, modified, or repealed.

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[3] According to a report prepared by LeAnn Luna and Matthew N. Murray for the State Tax Panel in October 2015: "…the number of Connecticut corporate taxpayers claiming credits has declined over the last decade, falling to 3,639 in 2012. However, the value of credits has trended up from $93.1 million in 2003 to $151.4 million in 2012, an increase of 62.6 percent. The value of credits carried forward to the 2013 tax year was a staggering $2.5 billion."

[4] For the most recent version, see: Office of Fiscal Analysis, "Connecticut Tax Expenditure Report," February 2016. https://www.cga.ct.gov/ofa/Documents/year/TER/2016TER-20160201_Tax%20Expenditure%20Report%20FY%2016.pdf

In addition, no policymakers are ever obligated to take action on the findings of the tax expenditure report. By statute, the Finance, Revenue and Bonding Committee is merely charged to "… meet to receive and analyze the report."[5] While normal appropriations are subject annually to the rigor of public hearings, expert testimony, and legislative deliberation, $6.4 billion in tax expenditures in the coming fiscal year are virtually ignored by the General Assembly. Not only does this process fail to hold tax expenditures accountable for the policy goals they were intended to achieve (such as economic development), it harms transparency in our budgeting process by effectively keeping this spending out of the public eye without opportunity to assess their opportunity costs.

We propose that the Committee consider the following reforms to ensure spending via our tax code is held to a similar level of accountability as appropriated spending:

Expand the Tax Expenditure Report. The biennial OFA Tax Expenditure report is an important step in promoting budget transparency. Just as this proposed bill expands the Tax Credit Report, we urge the Committee to do the same for the Tax Expenditure Report. We recommend the report:

- **Evaluate the extent to which each tax expenditure is meeting its policy goal**, including considerations of administrative cost, distributional impact, evolving fiscal climate, and expected change over time.
- **Submit a recommendation to continue, modify, or repeal each tax expenditure**, based on how well each tax expenditure is meeting its policy goal.

Bolster the legislative review process. Currently, the General Assembly is not obligated to act on the findings of the tax expenditure report. Requiring policymakers to treat over $6.4 billion in tax expenditures like normal appropriations will improve transparency and accountability.

- **Hold public hearings on the results of the Tax Expenditure Report,** so that taxpayers can weigh in on how public funds are used as they can during the regular appropriations process.
- **Require the General Assembly to vote on the recommendations of the tax expenditure report,** taking into account public testimony.

Thank you for your time. I would be happy to answer any questions.

Contact

Nick Defiesta
Associate Fiscal Policy Fellow
(203) 498-4240 x118
ndefiesta@ctvoices.org

[5] Public Act 97-316