



**STATE TAX PANEL**  
**OVERVIEW OF CONNECTICUT**  
**STATE REVENUE SYSTEM**

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# Outline of Presentation

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- I. Overview of Connecticut's State Revenue System
- II. Revenue Performance
- III. Revenue Volatility
- IV. Tax Incidence
- V. Impact of Tax Credits
- VI. Policy Changes 2000-2015



# Overview of State Revenue System

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- General Fund revenues are derived primarily from the collection of State taxes. Major taxes include:
  - Personal Income Tax
  - Sales and Use Tax
  - Corporation Tax
- In addition, the largest source of non-tax revenue to the General Fund is federal grants.
- The State has established a Special Transportation Fund for the purpose of budgeting and accounting for all transportation-related taxes, fees and revenues credited to such Fund.



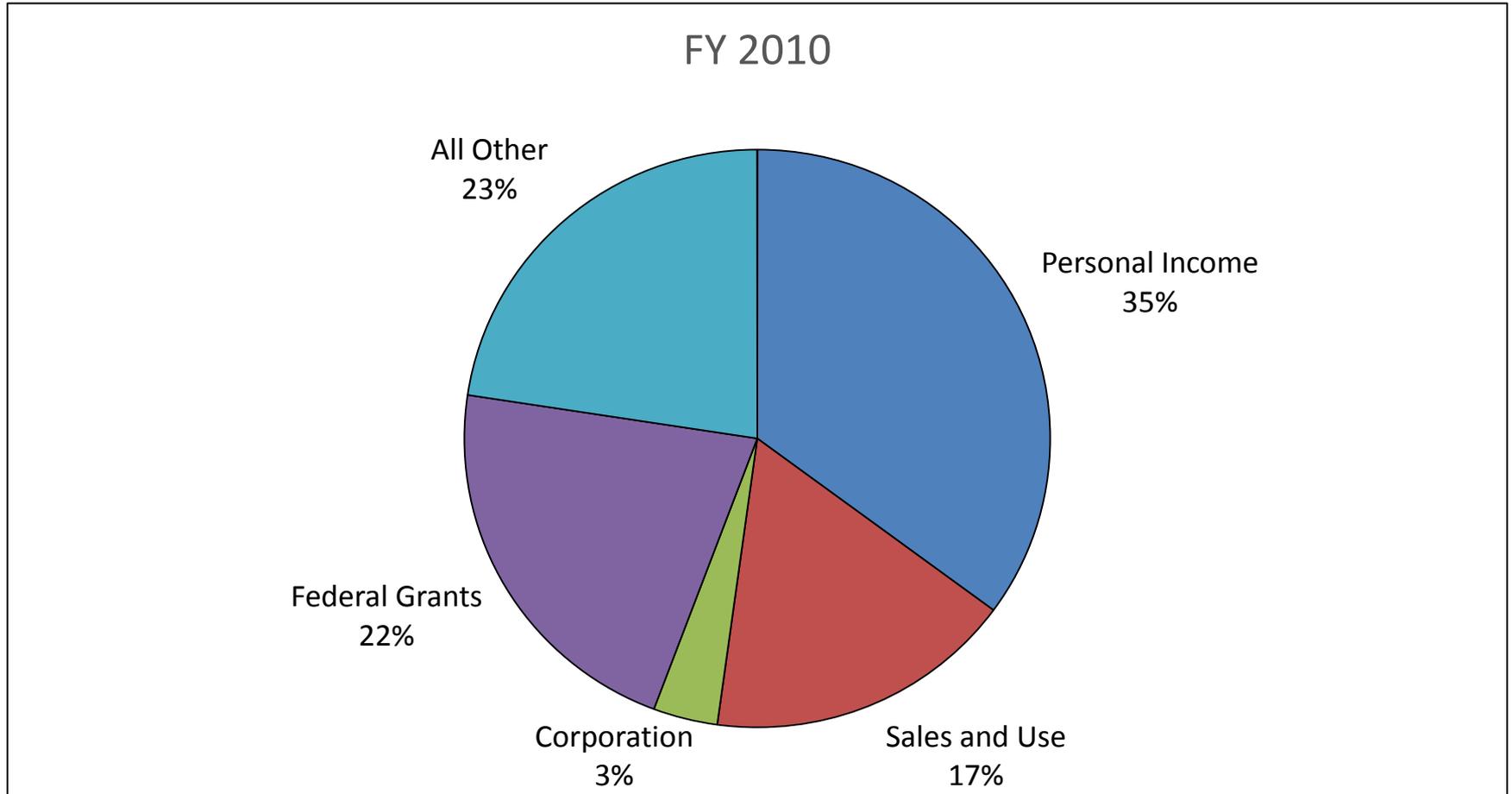
# Overview of State Revenue System

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- The following charts show the percent of General Fund revenue derived from the following sources:
  - Personal Income Tax;
  - Sales and Use Tax;
  - Corporation Tax;
  - Federal Grants; and,
  - All Other Sources
- Revenues are shown as a percentage of collections prior to refunds and net transfers to other funds.
- For comparative purposes, FY 2014 has been adjusted for net budgeting of Medicaid.



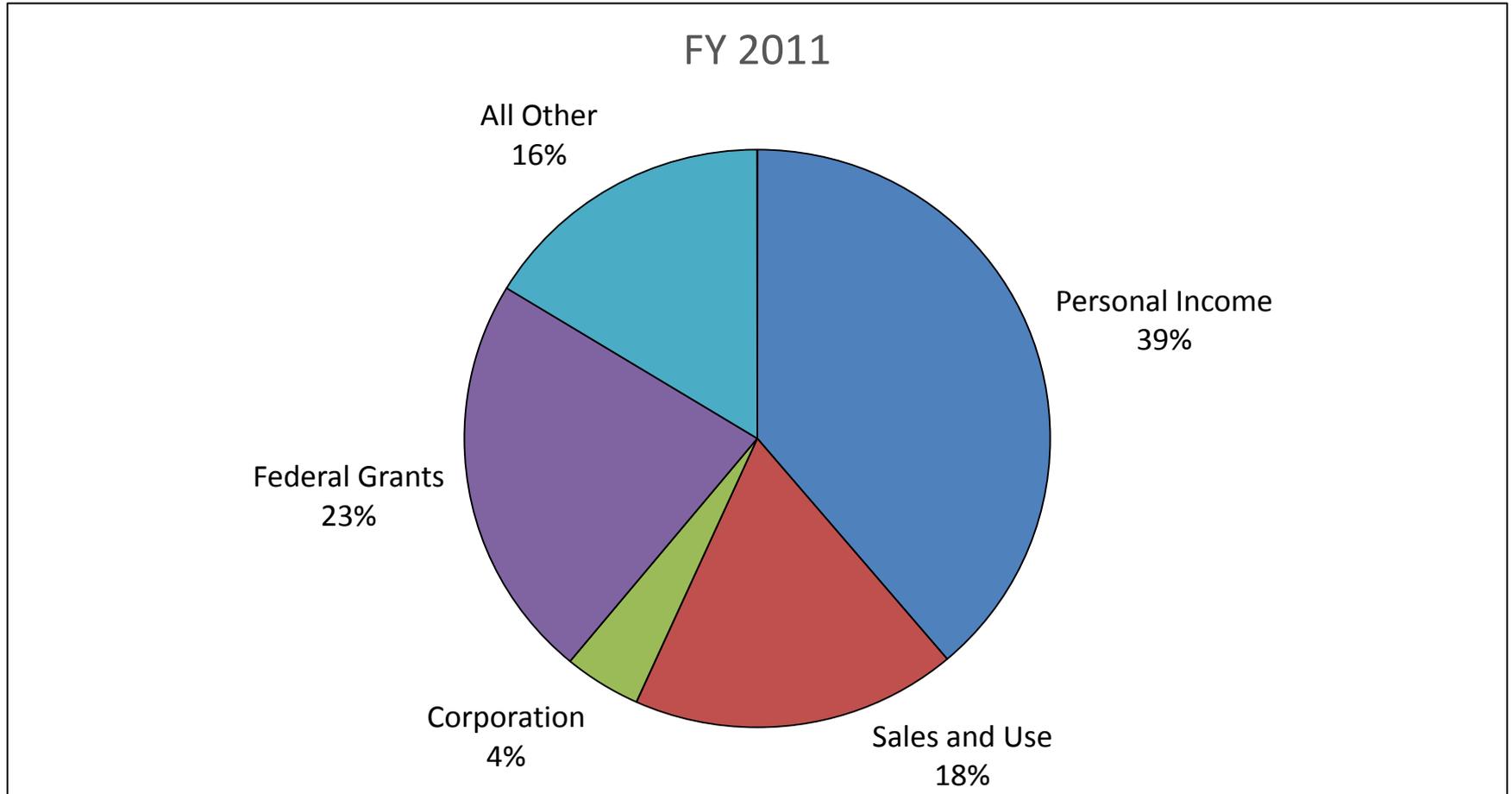
# Overview of State Revenue System



*Refunds reduced collections by \$1,072 million.*



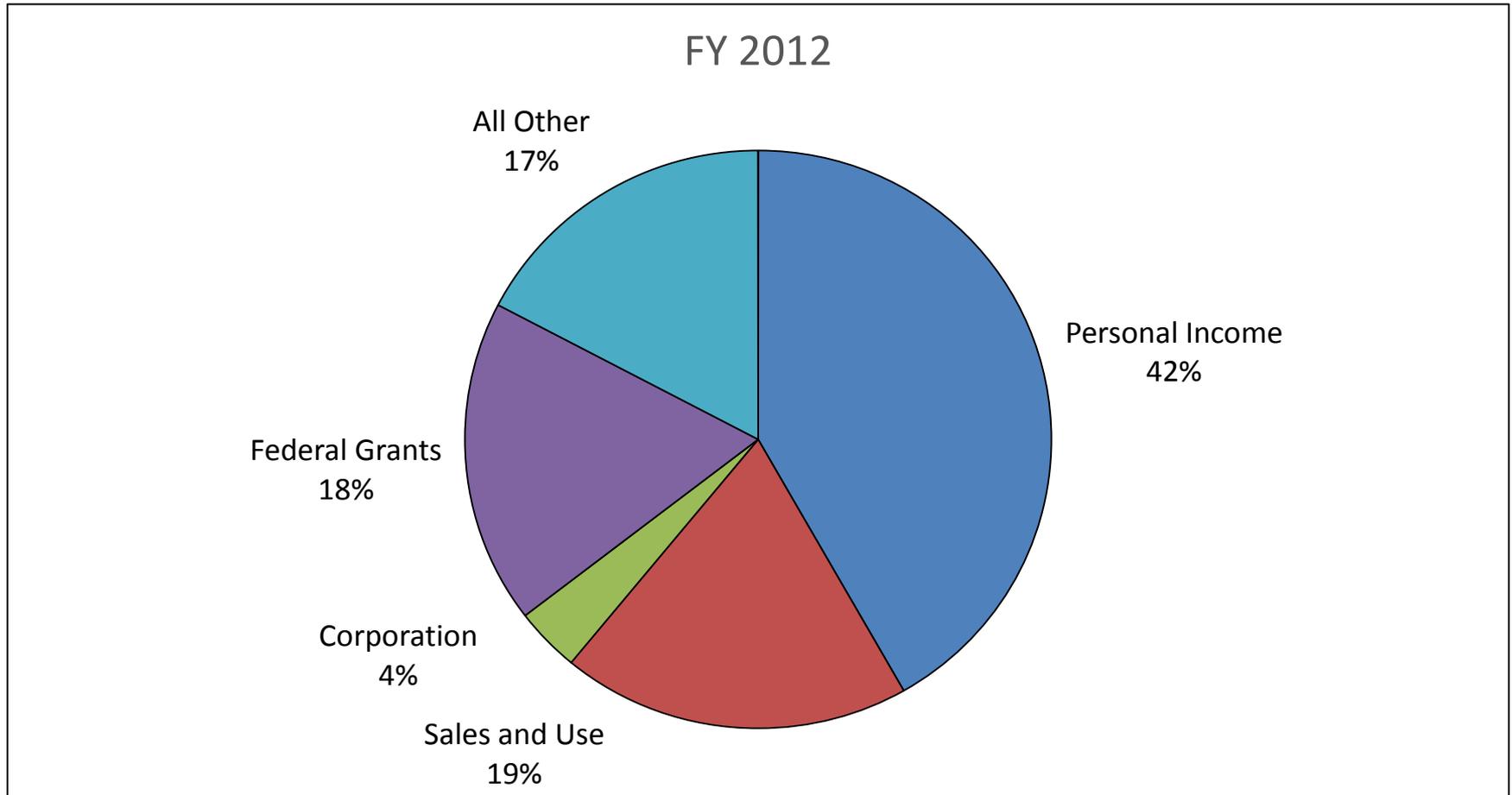
# Overview of State Revenue System



*Refunds reduced collections by \$967 million.*



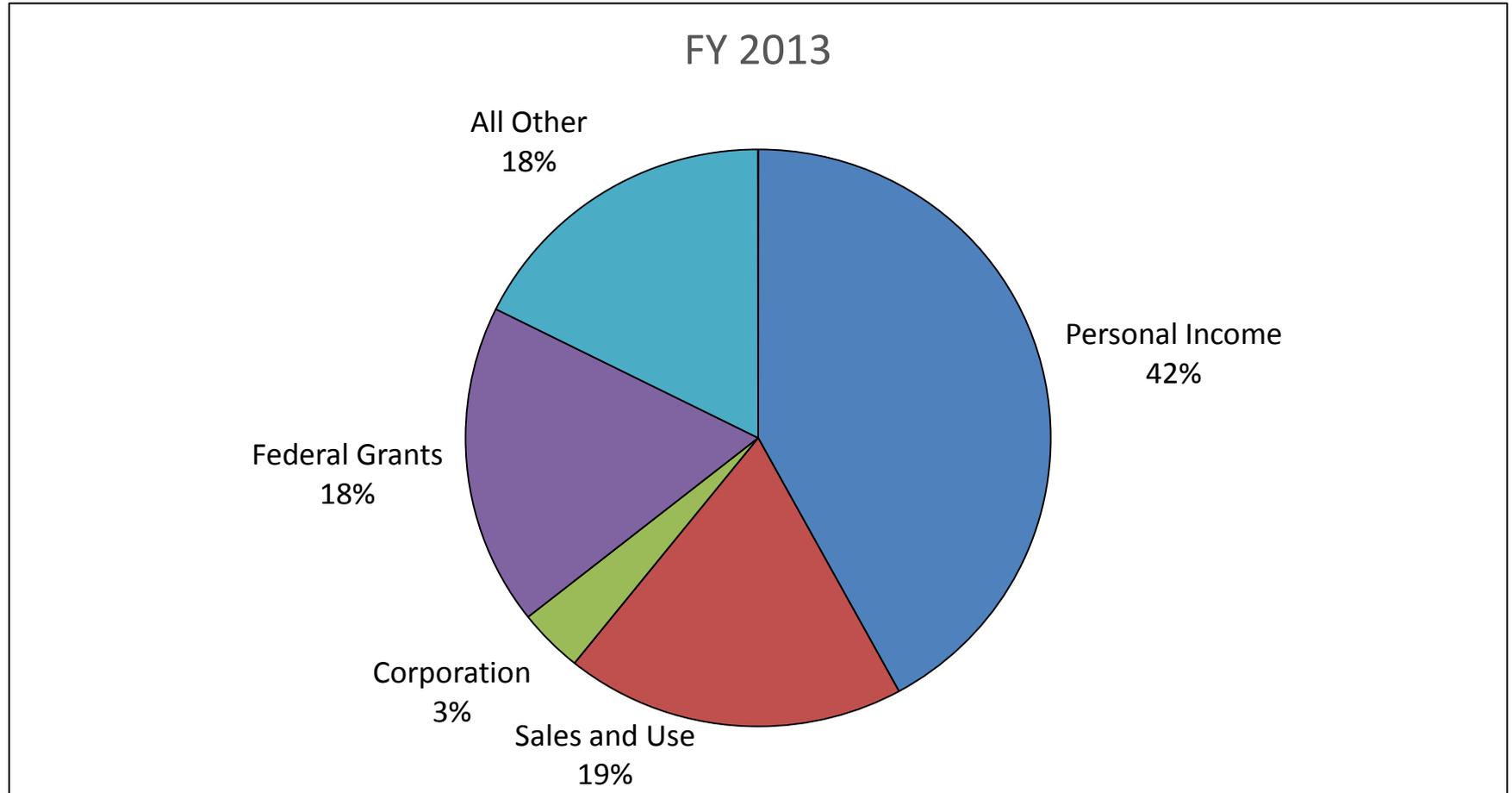
# Overview of State Revenue System



*Refunds and transfers reduced collections by \$1,348 million.*



# Overview of State Revenue System

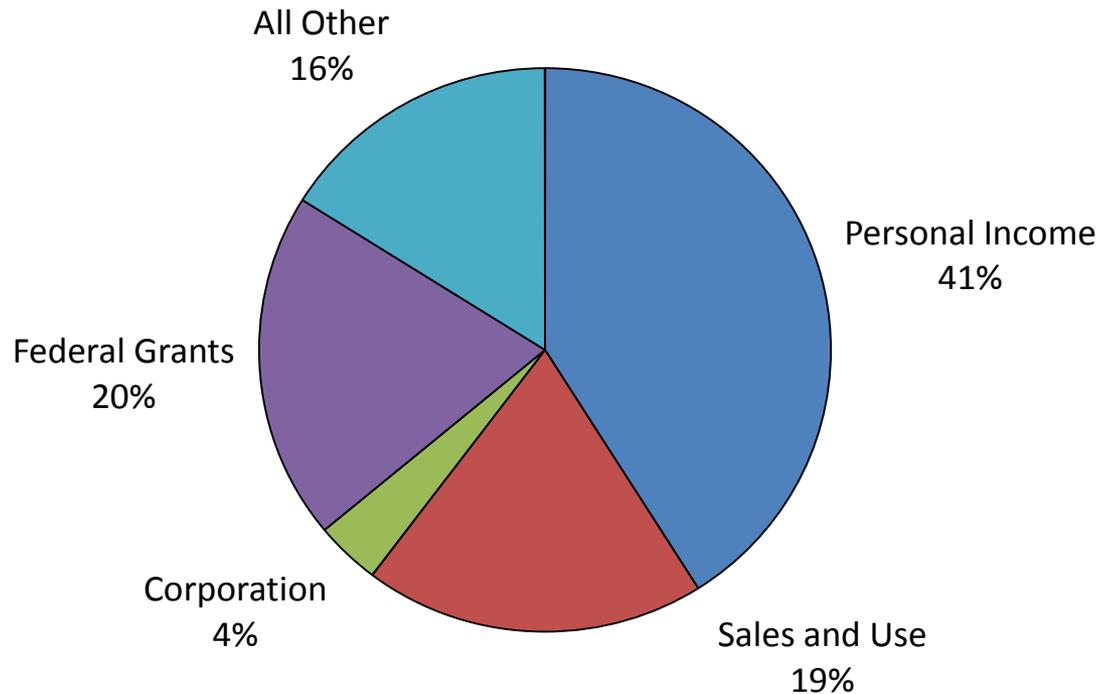


*Refunds and transfers reduced collections by \$1,351 million.*



# Overview of State Revenue System

FY 2014 – Adjusted for Net Budgeting of Medicaid\*



*Refunds reduced collections by \$1,072 million.*

*\*For purposes of this chart, \$2,993 million was added to Federal Grants in order to estimate what General Fund revenues would have been had the State of Connecticut not switched to net budgeting Medicaid in FY 2014.*



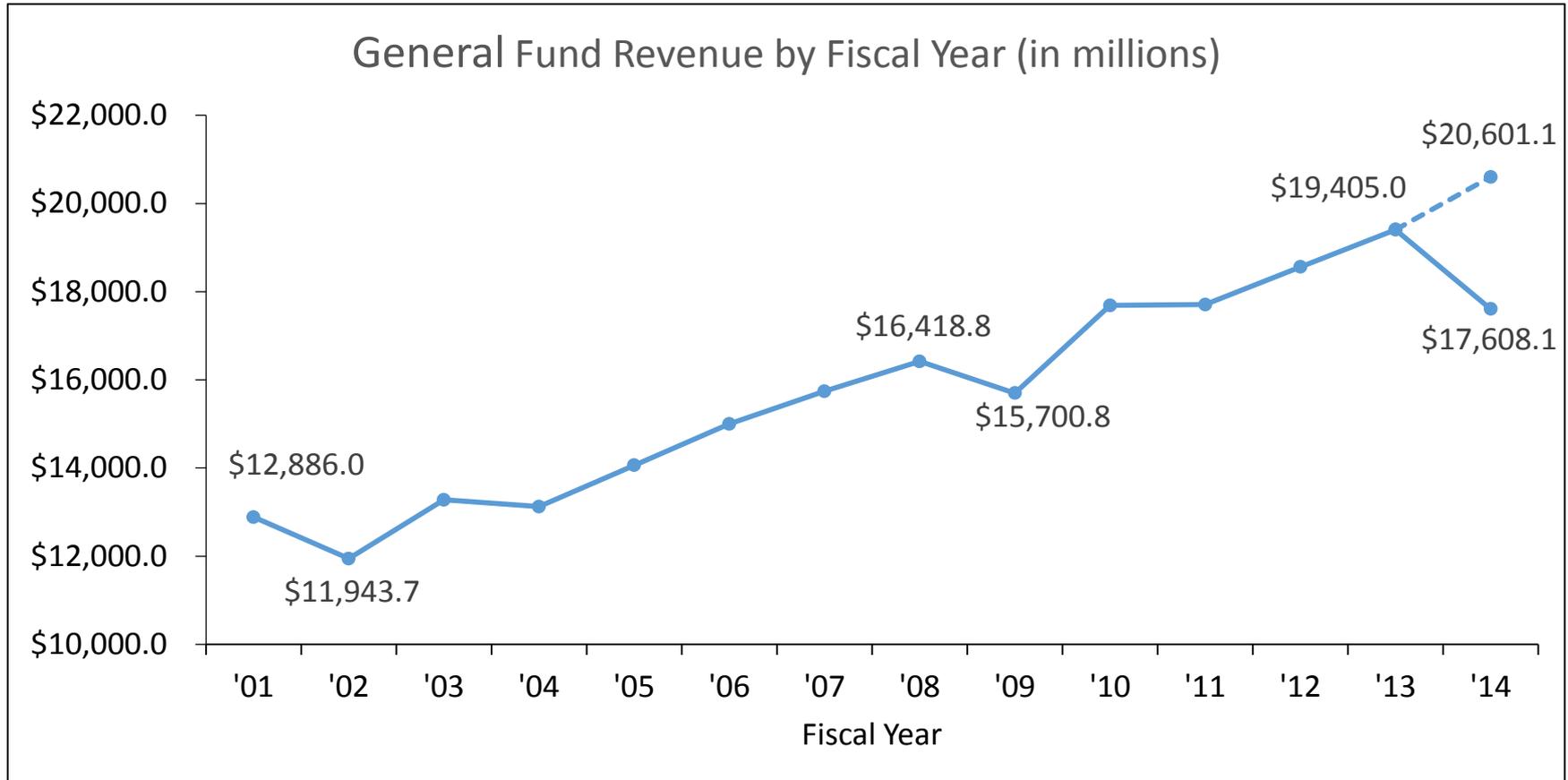
# Revenue Performance

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- General Fund revenue has grown in conjunction with the state economy, increasing during expansionary periods and decreasing during recessions.
- Revenues peaked in FY 2001 prior to the early 2000's recession.
- Revenues hit another peak in FY 2008 before entering into the Great Recession.
- The following graph shows historical General Fund revenue as reported in the Annual Report of the State Comptroller.



# Revenue Performance



Source: Office of the State Comptroller

Dashed line represents the revenue that would have been recorded as General Fund revenue in the absence of the move to net budgeting of Medicaid.



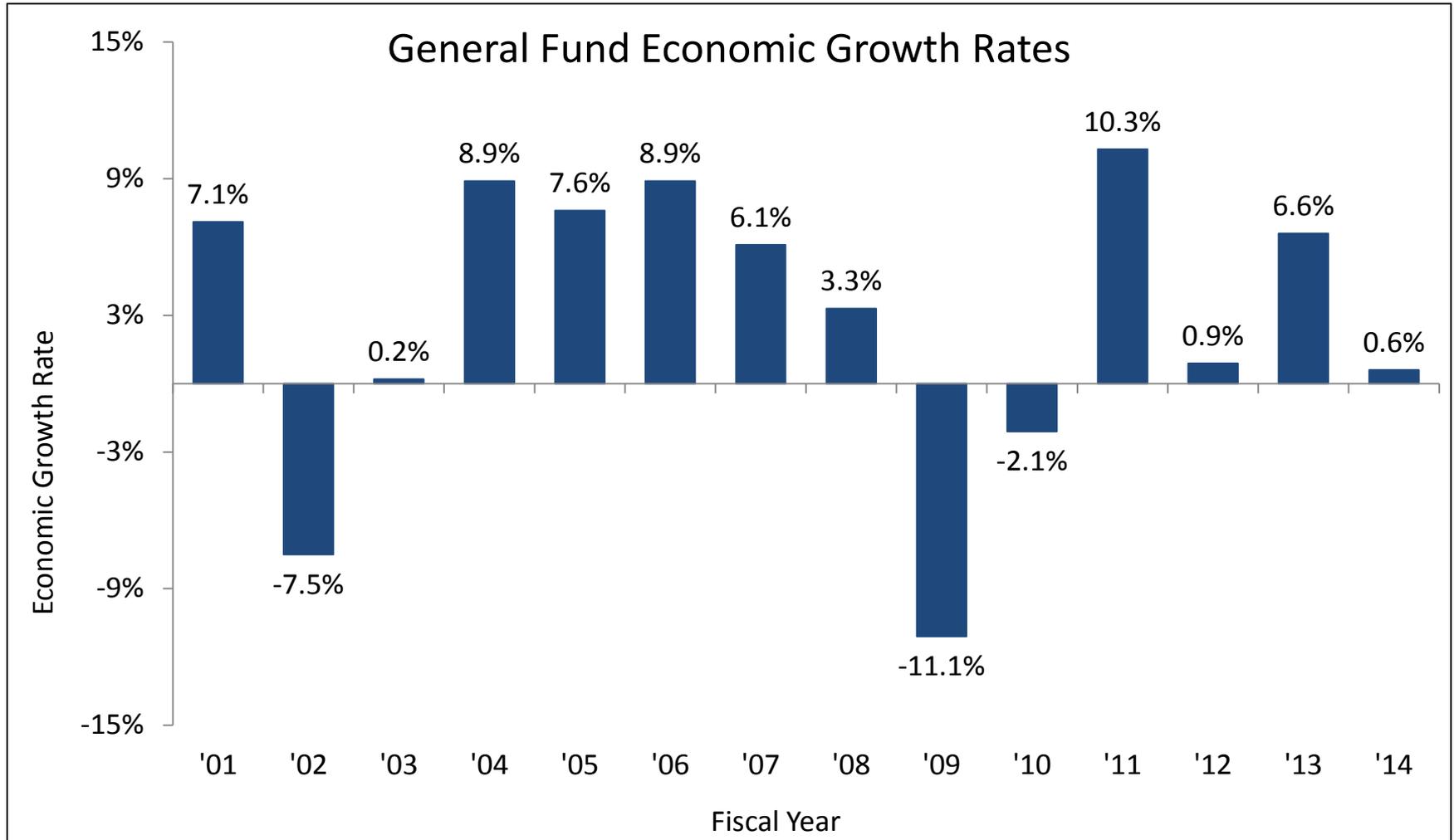
# Revenue Performance

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- The preceding chart represents nominal growth in General Fund revenue.
- However, tax policy changes over time have had a fundamental impact on revenue collections.
- OPM has estimated the “economic growth rate,” or baseline growth rate, of the General Fund and major sources by controlling for the estimated impact of policy changes.
- The following graphs show the economic growth rates for the General Fund, income tax withholding, income tax estimates and finals, and sales and use tax.

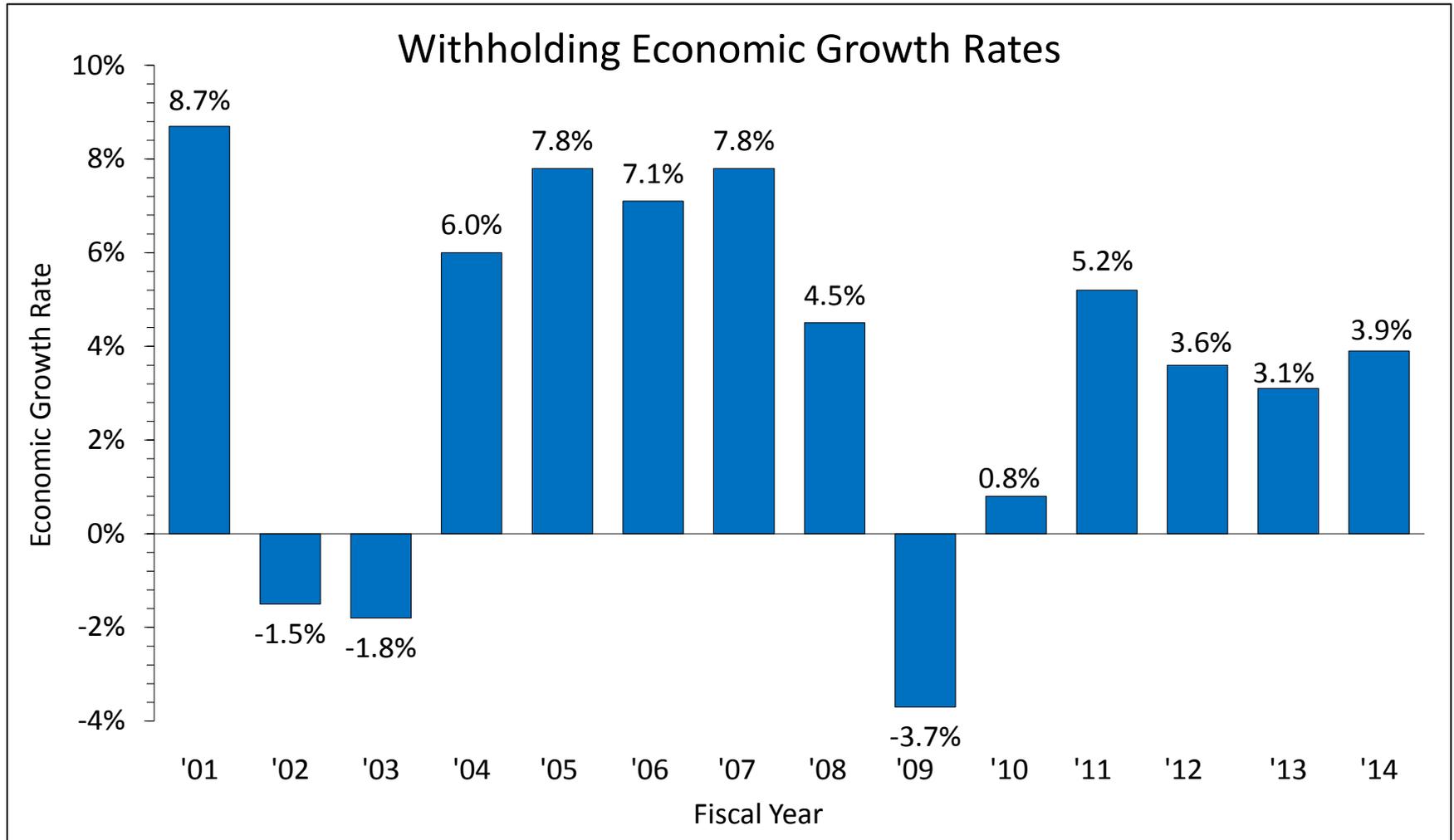


# Revenue Performance



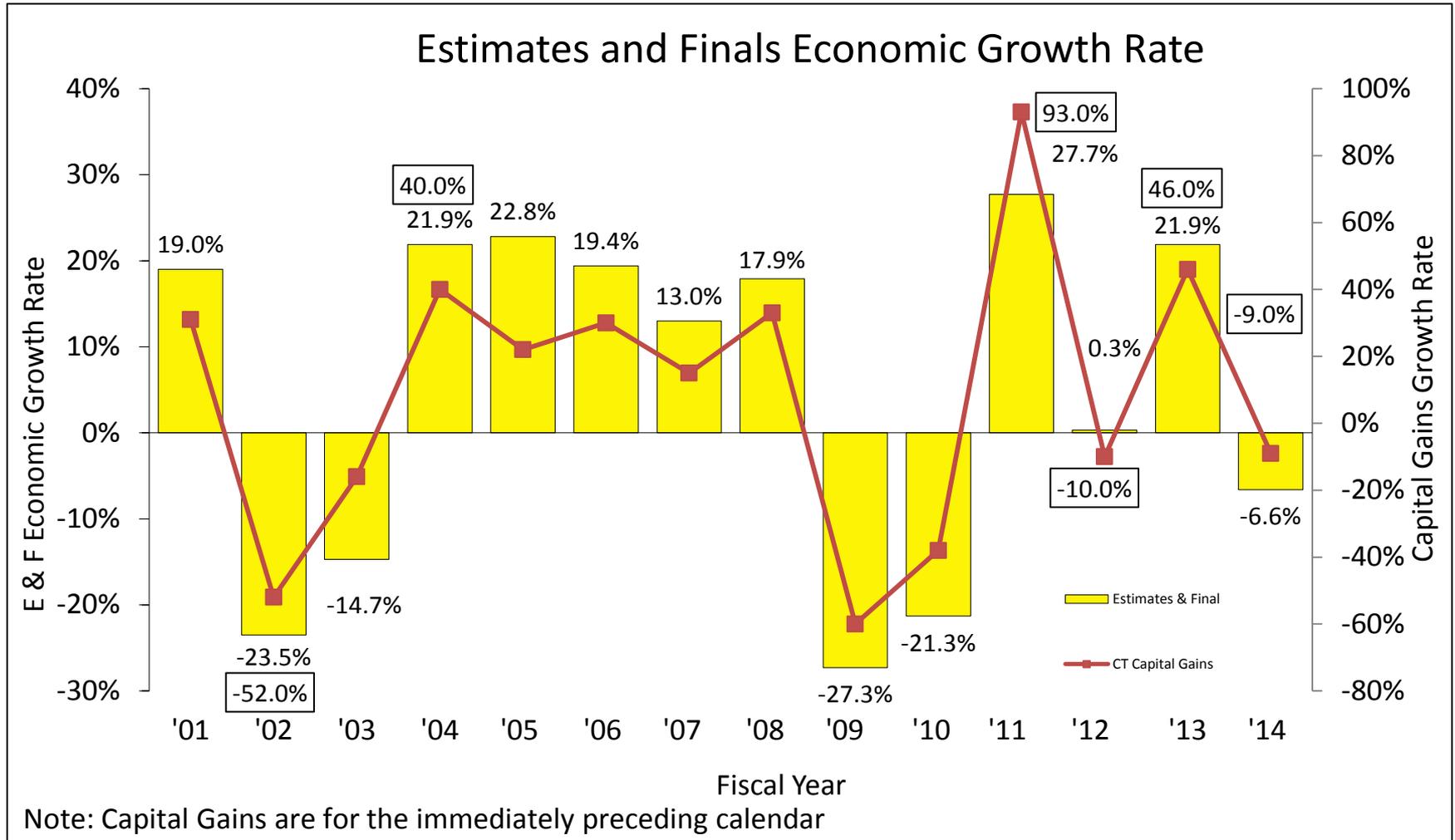


# Revenue Performance



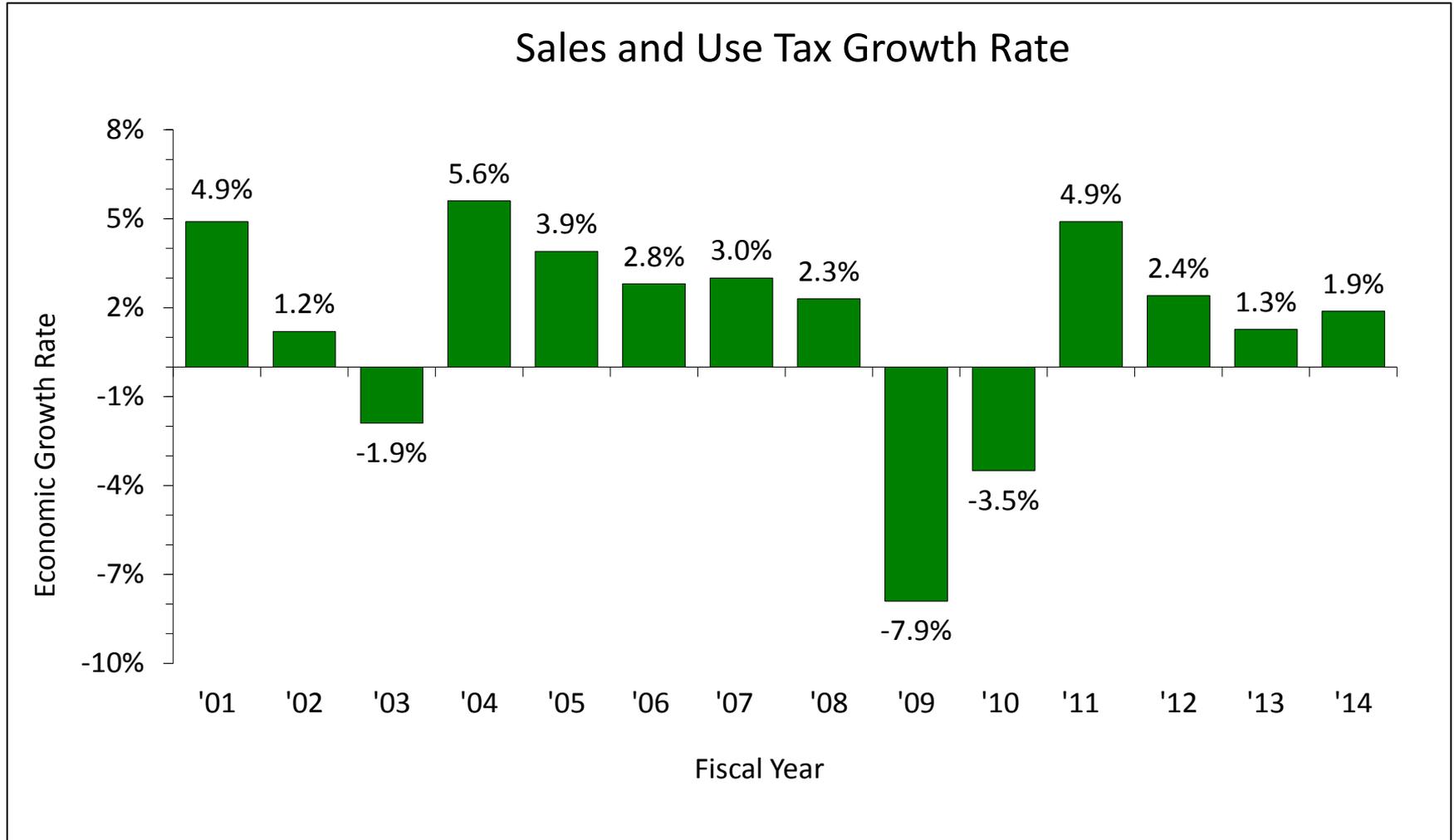


# Revenue Performance





# Revenue Performance





# Revenue Performance

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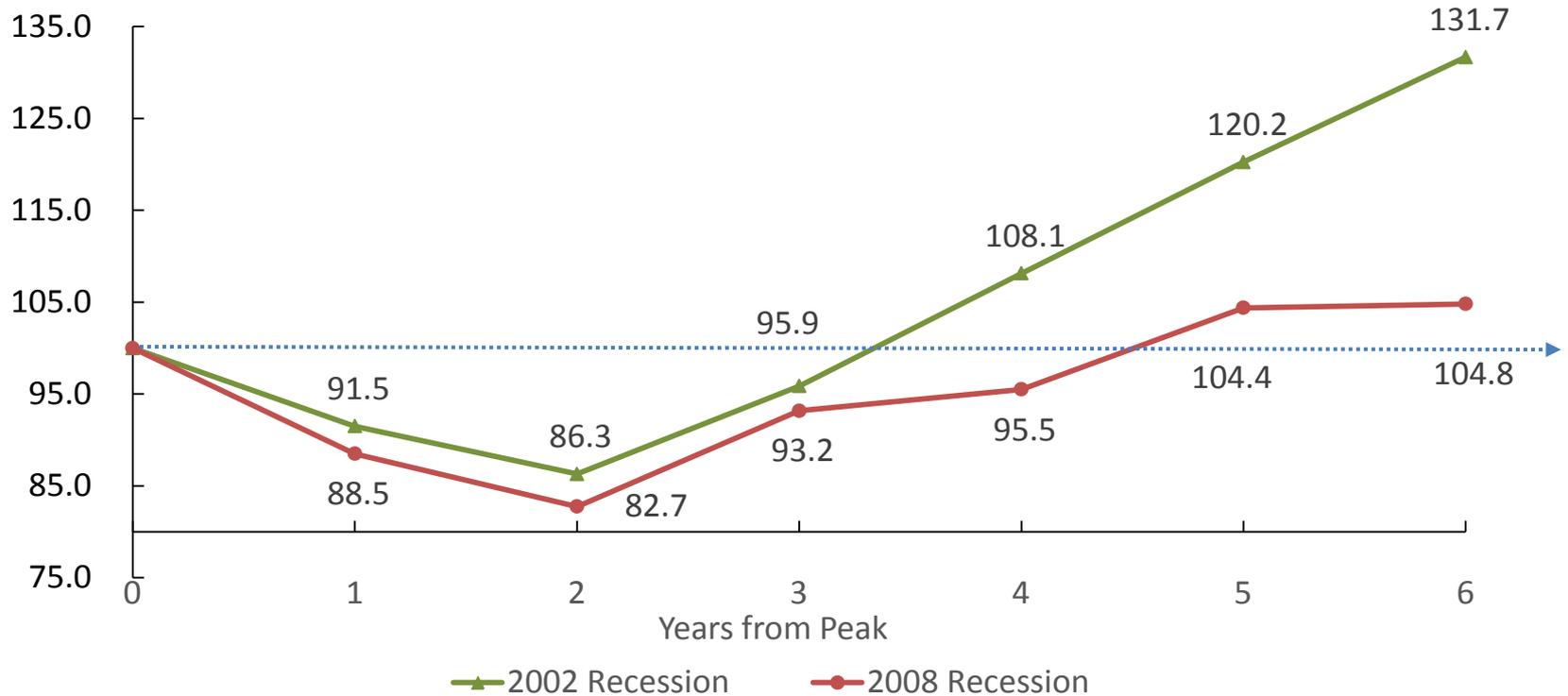
- The recovery of General Fund revenues following the Great Recession has been weaker and more uneven than prior recoveries.
- The following graphs compare the recoveries in Personal Income Tax and Sales Tax collections following the prior two recessions.
- The graphs set peak years (FY 2001 and FY 2008) to an index value of 100 and remove the impact of tax changes



# Revenue Performance

## Personal Income Tax Impact of Recessions on Baseline Revenue

Peak Years: FY 2001 & FY 2008

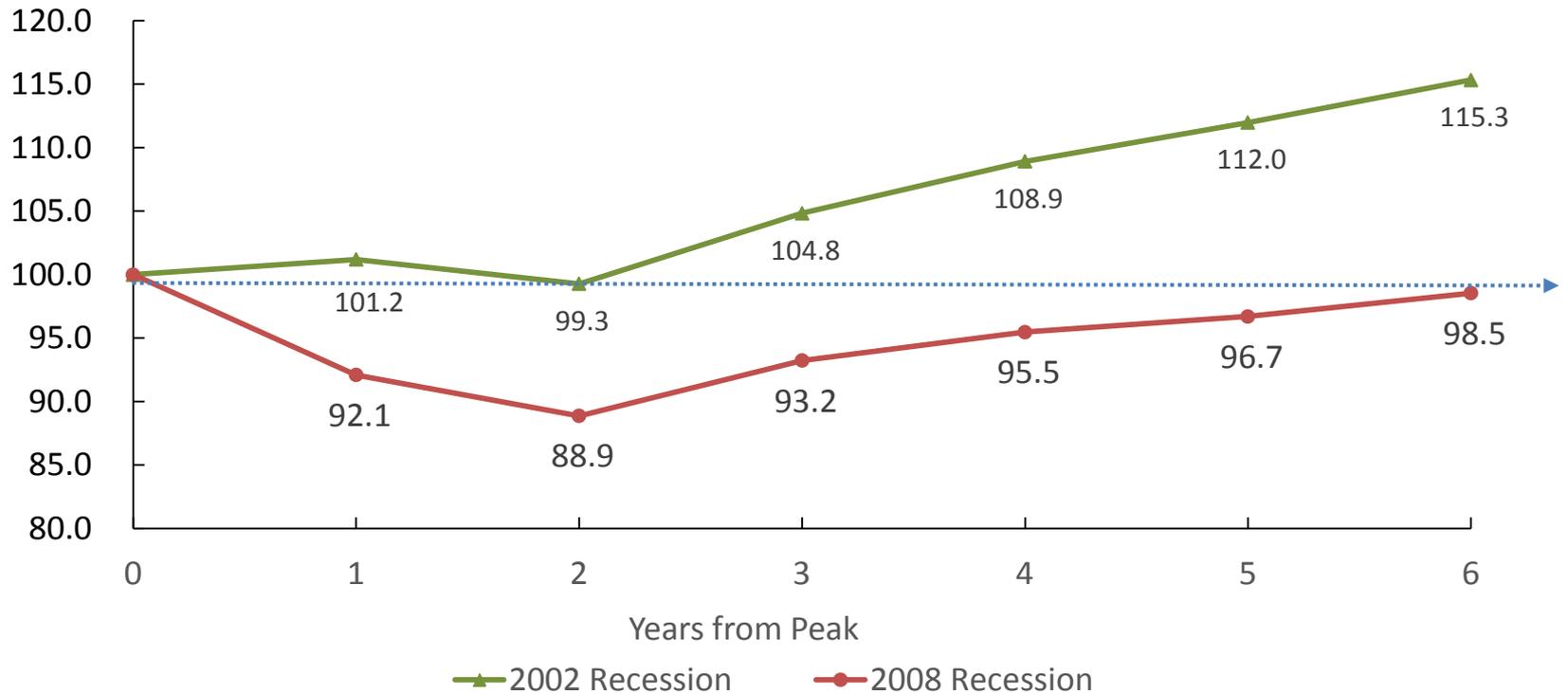




# Revenue Performance

## Sales and Use Tax Impact of Recessions on Baseline Revenue

Peak Years: FY 2001 & FY 2008





# Revenue Volatility

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- Each revenue source of the General Fund and Special Transportation Fund has a different base and is subject to different economic and behavioral phenomena.
- As a result, some revenue sources are more volatile than others.
- Greater volatility implies more difficulty forecasting future receipts and less reliability as changes occur in the economy.



# Revenue Volatility

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- Tax buoyancy is a common measure of revenue volatility.
- Buoyancy measures a revenue source's response to economic growth by comparing changes in tax receipts to changes in gross state product (GSP).
- Buoyancy models do not control for changes in tax policy – a major limitation to these types of models
- OPM has conducted tax buoyancy analyses of General Fund, personal income tax, sales and use tax, and corporation tax revenue.



# Revenue Volatility

	Buoyancy	Adjusted R-Square
General Fund	1.18	0.86
Personal Income Tax	1.80	0.92
Sales and Use Tax	0.60	0.66
Corporation Tax	1.43	0.66

- This indicates that a 1% change in Connecticut gross state product resulted in a 1.8% change in personal income tax, a 0.6% change in sales and use tax, a 1.4% change in corporation tax, and a 1.2% change in General Fund revenue during the period from fiscal year 2001 to 2014.



# Revenue Volatility

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- Public Act 15-244, the FY 2016-2017 biennium budget, included several reforms to the Budget Reserve Fund (BRF).
- The intent of these changes is to mitigate the revenue volatility which has led to budget uncertainty in the state in recent years.
- The bill requires that growth in “combined revenue” above a threshold be deposited to the Budget Reserve Fund beginning in FY 2021.
- “Combined revenue” means tax revenue from the estimated and final payments of the personal income tax and the corporation business tax.



# Tax Incidence

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- There is frequent discussion as to whether certain tax types are regressive, progressive, or proportional:
  - A tax is “progressive” if higher income earners pay more than lower income earners as a percentage of their income.
  - A tax is “proportional” if higher income earners and lower income earners pay a similar amount as a percentage of their income.
  - A tax is “regressive” if higher income earners pay less than lower income earners as a percentage of their income.
- In order to assess the equity of Connecticut’s tax system, the Department of Revenue Services published the Connecticut Tax Incidence study in December 2014.



# Tax Incidence

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- The Suits Index can be used to compare relative progressivity between taxes within Connecticut.
- The Suits Index is a nonbinary measure with a value between negative one and one where regressive taxes have negative values, progressive taxes have positive values and a proportional tax would be equal to zero.
- The degree of a tax's progressive or regressive nature increases the further it is from zero.
- The following table summarizes the Suits Index for the taxes studied in the report.



# Tax Incidence

Tax Type	Suits Index
Gift and Estate	0.76
Personal Income	0.11
Corporation Business	-0.02
Real Estate Conveyance	-0.14
Insurance	-0.35
Gross Earnings	-0.38
Local Property Taxes	-0.39
Sales and Use	-0.39
Excise	-0.67
<b>Total</b>	<b>-0.22</b>



# Tax Credits

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- In order to incentivize certain private sector behavior, Connecticut offers taxpayers various tax credits. These credits reduce a taxpayer's liability, and therefore reduce General Fund revenue.
- Lost revenue may be “made up” by either increases in taxes or decreases in appropriations.
- Connecticut's Department of Revenue Services (DRS) provides annual data on the amount of tax credits claimed against the corporation business tax and the insurance premiums tax by income year.



# Tax Credits

Type of Credit	Tax Credits Claimed	
	2012	2008-2012
Fixed Capital	\$63,125,737	\$358,236,881
Film Production*	\$76,567,036	\$298,633,051
Electronic Data Processing	\$19,421,533	\$118,537,600
Research and Experimental Expenditures	\$20,681,089	\$86,239,102
Urban and Industrial Site Reinvestment	\$16,598,275	\$54,045,821
Research and Development	\$5,516,301	\$25,715,841
All Other	\$16,147,798	\$88,532,982
<b>TOTAL</b>	<b>\$218,057,769</b>	<b>\$1,029,941,278</b>

*\*Includes film production infrastructure and digital animation credits.*

Source: DRS Annual Statement



# Tax Credits

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- Relative to corporation tax credits, the State of Connecticut offers few credits against the personal income tax. However, two major credits are:
- The Property Tax Credit. Approximately \$209 million in property tax credits were claimed in income year 2013.
- The Earned Income Tax Credit. Approximately \$96 million in earned income tax credits were claimed in income year 2013.



# Policy Changes 2000-2015

At the turn of the century, tax rates were significantly different from where they stand today. The impact of two major recessions, combined with rising costs for healthcare, education, and unfunded pension liabilities, resulted in numerous policy changes for the state. Some of the major revenue changes that have been enacted over the past 15 years include:

	2000	2015
Personal Income Tax Rates	3.0%-4.5%	3.0%-6.99%
Earned Income Tax Credit (% of Federal)	None	27.5%
Sales and Use Tax Rate	6.0%	6.35%
Corporation Tax Rate	7.5%	7.5%
Corporation Tax Surcharge	None	20%
Cigarette Tax (\$ per pack)	\$0.50	\$3.65
Oil Companies Tax	5.0%	8.1%
Motor Fuels Excise Tax (¢/Gallon)	32¢	25¢



Thank you for your attention this morning.  
Questions?