



“Who Pays?” How Our State and Local Tax System Burdens Connecticut’s Poor and Middle Class: Executive Summary

Douglas Hall, Ph.D. and Shelley Geballe, JD, MPH

Revised October 2008

A common measure of tax equity is the share of one’s income paid in tax as compared to other taxpayers. Measured by this metric, Connecticut’s state and local tax system is regressive. That is, our wealthiest families pay a much *smaller* share of their income in state and local taxes than do more than four in five other Connecticut families. Indeed, the Institute on Taxation and Economic Policy’s forthcoming *Who Pays* report¹ finds that Connecticut’s wealthiest 1% of families² pay *less than half* the share of their income in state and local taxes than do the poorer four fifths (80%) of Connecticut families, after federal income tax deductions for state income and property taxes are factored in (see table below).³

CT State and Local Taxes as Share of Family Income, by Income Category, 2006

Income category	State and local taxes % of family income
Top 1%	4.7%
Next 4%	7.3%
Next 15%	8.9%
Fourth 20%	9.6%
Middle 20%	10.2%
Second 20%	10.4%
Lowest 20%	10.9%

Source: Institute on Taxation & Economic Policy

Connecticut’s state and local tax system is regressive

- Lower and middle income families pay a larger share of their incomes in sales and property taxes than do higher income families. By comparison, higher income families pay a larger share of *their* incomes in income tax than do lower and middle income families. *In total*, however, the state’s wealthiest families pay a much smaller share of their income in state and

local taxes than do its middle and lower income families. Why? Connecticut’s personal income tax does not have a sufficiently progressive rate structure to offset the regressivity of the other two taxes.

- The wealthiest 1% of Connecticut’s families (with average income in 2006 of \$3.3 million) paid 4.7% of their income in state and local taxes (taking into account federal deductions). This was *less than half* the share of income paid in these taxes by the state’s middle-income families (10.2% of their average income of \$55,100) or the poorest 20% of families (10.9% of their average income of \$15,100).
- Connecticut’s state and local tax system is regressive even among the lowest 80% of families; the share of income paid in state and local taxes *declines* as total income *increases*.
- Some assert that Connecticut’s wealthiest families pay *more* than their fair share of tax, citing the income tax they paid as a share of total state income tax revenues. While Connecticut’s wealthiest residents *do* pay a large share of Connecticut’s total income taxes, this reflects the fact that they report a large share of the total income in the state, *not* that they are taxed far more heavily on that income. In 2006, the top 1% of taxpayers in Connecticut (those reporting income of \$750,000 or more) paid 33% of the state’s total income taxes, but also reported 31% of the state’s total income.⁴ The top 6% of taxpayers (with income of \$200,000 and up) paid 53% of state income taxes, and reported 48% of the state income.
- Connecticut’s highest income families -- those in the top 1% -- pay a substantially smaller share of their income in combined state and local taxes than do their counterparts in Connecticut’s neighboring states: 6.4% in Connecticut,

compared to 6.7% in Massachusetts, 7.0% in Rhode Island, 7.9% in New Jersey, and 10.6% in New York (before federal deductions).

Toward a More Equitable Tax Structure

To make Connecticut's state and local tax structure fairer, Connecticut should:

Provide additional state aid to Connecticut's cities and towns to reduce Connecticut's relatively high property taxes.

Providing full funding for the Payment in Lieu of Taxes program and increasing the state's share of K-12 education funding to close to 50% would reduce the pressure on our local property tax; reductions in local property tax would provide particular benefit to our middle-income families and to small, start-up businesses.

Increase the share of income paid in tax by our wealthiest families. The Institute on Taxation and Economic Policy (ITEP) has modeled the impact on Connecticut's tax structure of adopting a top income tax bracket of 6% applied to the income of married couple families over \$200,000 and to the income of single filers over \$100,000. This new tax rate would result in the wealthiest 1% of Connecticut families paying an additional 0.64% of their income in state personal income tax, bringing the total share of their income paid in state and local tax to 7.0% before the federal offset. The next wealthiest 4% of families would pay an additional 0.06% of their income in tax, increasing the total share of their income paid in state and local taxes to 8.4% before the federal offset.

ITEP estimates that adding this 6% top bracket to Connecticut's income tax would generate approximately **\$470 million** in additional revenue, while **affecting only 7%** of Connecticut taxpayers. Notably, *even with* this rate increase, the share of income paid in state and local taxes by Connecticut's wealthiest 5% would *remain smaller* than what is paid by the "bottom" 95% of Connecticut families. That is, this change would only begin to close the gap in relative tax burden between Connecticut's low- and middle-income families and its wealthiest families.

Adopt a state earned income tax credit and increase Connecticut's personal exemptions. Another way to make Connecticut's tax structure fairer is to adjust the tax

burden at the other end of the income distribution by adopting a refundable state earned income tax credit (EITC) and increasing Connecticut's personal exemptions to account for inflation.⁵

Both measures would help compensate for the fact that Connecticut's tax threshold – the income level at which families begin to pay the state personal income tax – has not changed since the tax was adopted in 1991. As a result, more low-income families are becoming subject to the tax. An increase in the personal exemptions merely to keep pace with inflation would reduce the tax burden on many low and low-middle income families.

Further, for tax year 2007, a 20% refundable state EITC would have reduced the *total* state and local taxes of families with incomes between \$12,000 and \$17,000 by \$940, and would have reduced by a lesser amount the *total* state and local taxes of families with incomes under \$40,000.

This report is produced with the support of the Stoneman Family Foundation and the Melville Charitable Trust, and is released in cooperation with the Institute on Taxation and Economic Policy (ITEP). The contents of this report are the responsibility of Connecticut Voices for Children. The full report (with complete references) is available at www.ctkidslink.org.

¹ The Institute on Taxation and Economic Policy, *Who Pays?: A Distributional Analysis of the Tax Systems in All 50 States* (3rd Edition, 2008)(forthcoming).

² These data are based on the total income of non-elderly families (singles and couples, with and without children) because state tax systems often treat elderly families very differently than non-elderly families.

³ Because state income and local property taxes can be deducted in calculating federal income tax liability, the net financial impact of these taxes on a state taxpayer is reduced.

⁴ CT Department of Revenue Services, 2006 Personal Income Tax data, analyzed by Connecticut Voices for Children. Income figures refer to CT Adjusted Gross Income.

⁵ With one exception, Connecticut's personal exemptions (which are based on taxpayer filing status) have not been increased since the personal income tax was adopted in 1991. Public Act 99-173 included a phased-in increase in the exemption for single filers from \$12,000 in 1999 to \$15,000 in 2007. When the recession began in 2002, however, the phase-in was delayed by a total of four years; the standard deduction for single filers in this 2008 tax year is \$13,000 and will increase annually until it reaches \$15,000 in tax year 2012. However, the standard deductions for heads of households (\$19,000) and married couples filing jointly (\$24,000) have not been increased since the income tax was first adopted. If they had been increased simply at the rate of inflation, they would have been, in 2007, \$29,786 for head of household filers, and \$37,625 for married couples filing jointly (and \$18,812 for single filers).