CONNECTICUT VOICES FOR CHILDREN
Independent research and advocacy to improve the lives of Connecticut's children

Testimony Regarding
S.B. 946: An Act Concerning Revenue Items to Implement the Governor's Budget

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Committee on Finance, Revenue, and Bonding
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Senator Frantz, Representative Davis, and distinguished members of the Finance Committee:

My name is Kenneth Feder, and I am a policy analyst with 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.

Connecticut Voices for Children *supports* raising additional revenue through (a) eliminating outdated sales tax exemptions, (b) increasing the progressivity of the State income tax, and (c) closing corporate tax loopholes, as proposed in S.B. 946. Additional revenue is needed to preserve essential State investments in children, and these proposals would raise that revenue in a way that increases the fairness of the State tax code.

Connecticut Voices for Children *opposes* delaying for another two years full restoration of the Earned Income Tax Credit (EITC). We urge the Committee to reject this delay, and provide working families their promised tax break.

To close the State's budget deficit, the Governor's Proposed Budget would impose disproportionate and painful cuts on investments in our children's future well-being. To assess the impact of the budget on children, Connecticut Voices for Children developed the Children's Budget: a compilation of all major line-items that support children and families. The Governor's Budget would reduce current services funding for line-items in the Children's Budget by $313 million, a cut of 5.1%. In fact, while investments in children make up about a third of state spending, reductions to investments in children make up more than half of all general fund spending cuts in the Governor's budget proposal. Among the most painful of these cuts, the Governor proposes:

- Eliminating HUSKY health insurance coverage for 34,000 pregnant women and parents;
- Reducing Medicaid payments to healthcare providers who serve low-income children and families, including a cut of $2.6 million to OBGYN providers;
- Reducing funding for public higher education by ten percent;
- Reducing State support for Voluntary Services for developmentally disabled children with co-occurring mental and behavioral health challenges by sixty percent;
- Imposing $157 million in cuts to numerous K-12 education programs, and providing no increase in general education aid to any town.

Simply put, these cuts are shortsighted, and ask the most from those who can least afford to give. They would limit families' access to needed medical care and curtail educational opportunities for Connecticut students, setting our children and youth up for poor health, education, and economic outcomes in adulthood, and jeopardizing the vitality of our state's future workforce.

The budget proposed by the Appropriations Committee would restore many of the most painful cuts to children. The Appropriations' Committee's proposed budget would:

- Restore HUSKY health insurance for 34,000 low-income parents and pregnant women;
- Lessen by $43.5 million the Governor's proposed cut to higher education;
- Eliminate most of the Governor's proposed cut to Voluntary Services for developmentally disabled youth;
- Lessen the Governor's proposed cut to Medicaid provider reimbursements, including OBYN providers; and
- Restore partial or full support for many programs critical to children and families, including Community Plans for Early Childhood, Parent Trust Fund, Improving Early Literacy, Family Resource Centers, Bridgeport's ABCD Total Learning Initiative, the Children's Trust Fund (Help Me Grow, Family School Connection, Family Empowerment Programs), and more.[1]

In total, the Appropriations Committee proposal would restore $130 million in funding to children's programs relative to the Governor's proposal.

Many of the priorities funded in this budget have bipartisan support, and are also funded in the Republican Blueprint for Prosperity Budget Proposal.[2] These include restoring HUSKY coverage for pregnant women, restoring funding for Voluntary Services, and restoring funding for the Parent Trust Fund. In fact, in some areas, the Republican proposal would wisely go further, rejecting proposed cuts to the Department of Children and Families (DCF), and funding further independent oversight of that agency.

In order to preserve the essential investments in children supported in the Appropriations Committee Budget, the Republican Blueprint for Prosperity, or both, additional revenue is required. Connecticut's budget deficit is driven principally by two factors: the need to pay down significant bonded and pension debt (which was worsened by the Great Recession); and the aging of our State's population which increases the cost of healthcare for employees (current and retired) and HUSKY members. Undoubtedly, better decisions could have been made over the past two decades: to appropriately fund State Employee Retirement System; to save more for a rainy day so as to avert some of the need to issue economic recovery notes during recessions; and to save more for healthcare costs. But these are the debts we have incurred, and we must not allow them to crowd out our most important public investments; **our children should not be asked to bear the burden of past poor decisions.**

The Finance Committee's revenue proposal takes three common sense steps to raise revenue needed to restore investments in children:

1. **Eliminating outdated tax expenditures.** The Finance Committee would eliminate an existing partial exemption to the sales and use tax for computer and data processing services, and begin treating web hosting, creation, and development services similarly to other computer and data processing services. These exemptions were created in the mid-nineties at the dawn of the internet-driven tech revolution as incentive for this industry.[3] Now, the special tax treatment for these services is outdated. The Office of Fiscal Analysis (OFA) estimates eliminating these exemptions would raise $162.8 million in FY16 alone, an amount equal to more than half of the Governor's proposed cuts to the Children's Budget.

2. **Increasing the progressivity of our State's tax code.** The Finance committee would increase the top marginal income tax rate for high earners from 6.7% to 6.99%, and establish an additional 2% tax on high earner's capital gains. These changes would affect only joint filers with income over $1 million, single filers with income over $500 thousand, and heads of household with income over $800 thousand, and would have no effect on more than 95% of Connecticut taxpayers. Because State personal income tax can be deducted from federal taxes, these high earners would recover close to half of this loss, on the federal government's dime. Our highest tax rate would remain below New York, New Jersey, and Vermont. Connecticut's tax code is currently extremely regressive: according to the most recent analysis by the Department of Revenue Services (DRS), in 2011, the wealthiest ten percent of Connecticut households paid only about 8.2 percent of their income in taxes, while average households paid almost 11.6 percent of their income in taxes, and the poorest 300,000 households paid more than 26 percent of their income in taxes.[4] Rather than asking these already overtaxed low- and middle-income families to bear the burden of the State's budget woes through cuts to the healthcare and public universities they depend on, it is more appropriate to simply ask our State's wealthiest to pay their fair share. Together, OFA estimates the two proposed income tax changes would raise $280.4 million in new revenue in FY16, and amount equal to more than three-quarters of the Governor's proposed cuts to the Children's budget.

3. **Closing a corporate tax loophole that favors large multistate corporations over small businesses.** The Finance Committee would institute mandatory combined reporting of multi-state corporate income and expenses. This would close an existing tax loophole that allows large companies conducting business in multiple States to use accounting gimmicks to avoid paying Connecticut taxes. This loophole currently gives multistate corporations an unfair advantage over small businesses that only conduct business in Connecticut. The Office of Fiscal Analysis estimates this reporting change would raise $38.6 million in new revenue, revenue that Connecticut should already be collecting anyway.

Two other significant revenue changes should be noted: The Finance Committee would support the Governor's proposal to restrict the ability of corporations to carry forward net operating losses to reduce tax liability in the following year. The Committee also would broaden the sales tax base to include many more services, lower the overall rate, and remit additional revenue to towns through the Payment in Lieu of Taxes (PILOT) and Municipal Revenue Sharing Account (MRSA) programs as dictated by S.B. 1, to help reduce property taxes and equalize liability across towns. We support measures that raise sufficient revenue to adequately fund the State's investment in children; we do not have a position on these two specific proposals at this time.

The Finance Committee's support for the Governor's proposal to raise revenue by delaying for two years full restoration of the State EITC is misguided, and should be rejected. The EITC is a credit claimed by low-income families against taxes on earned income. It has proven to be one of the State's most effective anti-poverty programs. In 2013, 190,000 Connecticut filers claimed the State EITC. These filers had an average household income of $18,000 per year, and received an average tax break of $426. There were EITC claimants in every one of Connecticut's 169 towns. The EITC can only be claimed by people who earn income through work, and a worker's credit grows with each additional dollar of earnings, creating a strong incentive to enter the workforce. Simply put, the EITC makes work pay, and helps families make ends meet.

Delaying restoration of the EITC is *not* asking everyone to pay their fair share to close the budget deficit; it is asking low-income working families to pay more than their fair share. As already noted, the average EITC claimant earned $18,000 in 2013. According to DRS, a Connecticut family with income in this range pays about 18 percent of its income in state and local taxes, higher than the average rate in Connecticut (11.57%), and more than double the rate paid by the wealthiest tenth of residents (8.18%). In FY 2015, Connecticut's EITC was scheduled to be restored to its original amount, 30 percent of a filer's federal credit amount. Delaying this proposal would impose an $11 million tax increase on these low-income working families who already pay more than their fair share in taxes.

The Governor's budget proposal would balance the budget by imposing painful cuts that jeopardize the health, education, and well-being of thousands of Connecticut children. Connecticut has a better choice: preserving essential investments in children by taking commonsense measures to raise new revenue. **We urge the General Assembly to support revenue options, such as those in S.B. 946, that eliminate outdated tax expenditures, increase the progressivity of the State's tax code, and close corporate tax loopholes, and to use this revenue to preserve investments in children and their families.**

Thank you for your time, and we welcome your questions.

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[1] An explanation of these line items can be found in the Department of Education, Office of Early Childhood, and Department of Social Services budgets.
[2] See "Blueprint for Prosperity: Connecticut Republican Budget Plan FY2016 – FY2017," April 24, 2015. Available at http://www.hartfordbusiness.com/assets/pdf/HB10925424.PDF.
[3] "Connecticut Tax Expenditure Report," Office of Fiscal Analysis. January, 2014. Available at http://www.osc.ct.gov/openCT/docs/Tax%20Expenditure%20Report%20FY%2014.pdf.
[4] "Connecticut Tax Incidence," *Department of Revenue Services*. December, 2014. Available at http://www.ct.gov/drs/lib/drs/research/drstaxincidencereport2014.pdf.