BOLSTERING STATE ECONOMIES BY RAISING PROGRESSIVE TAXES

ISSUE BRIEF BY **KITTY RICHARDS** | JULY 2020

EXECUTIVE SUMMARY

As state and local governments face unprecedented revenue shortfalls over the next three fiscal years, many are considering slashing services and public sector employment at exactly the time they are needed most. These moves have the potential to devastate communities and local economies, causing unnecessary hardship, deepening the recession, and hampering the eventual economic recovery. The federal government should step in immediately, using cheap federal borrowing to support state and local governments—just as the recently passed House stimulus bill (the HEROES Act) would do. But states and localities should also move quickly to stave off cuts and *expand* services and employment by raising revenue progressively.

THE CASE FOR RAISING PROGRESSIVE TAXES AT THE STATE AND LOCAL LEVELS

State Policymakers Are Proposing Devastating Cuts to Services and Jobs to Close Massive Revenue Shortfalls

State and local governments across the United States are currently facing unprecedented strains on their budgets due to the COVID-19 crisis. They are on the frontlines of medical care, public health, economic regulation, and the social safety net as the nation battles a deadly pandemic and unemployment levels not seen since the worst of the Great Depression. At the same time, revenues have collapsed with the economy. Recent projections show large state and local budget shortfalls, with one estimate placing state shortfalls alone at $615 billion through July of 2022 (McNichol and Leachman 2020), and another projecting state and local revenue shortfalls of nearly $900 billion just through December 2021(Bartik 2020).

The federal government should step in immediately. The latest House-passed stimulus bill, the HEROES Act, would provide states and localities with $1 trillion in federal aid,[1] which could save millions of jobs and ensure that Americans continue to receive vital services and supports.

But states and localities must act. Forty-six states began their new fiscal year on July 1 (NCSL 2020), and almost all are constrained by some type of balanced budget requirement (NCSL 2010), forcing them to close shortfalls for the current fiscal year and next fiscal year quickly and to begin planning for the following fiscal year's large shortfalls.

This has led to catastrophic budget *cuts* when increased services are needed more than ever.[2] Across the country, governors and legislatures have begun enacting austerity budgets that will hamper their ability to fight the virus and restart economic activity, deepen inequality, and lead to poverty, hunger, and deprivation for millions.

States Can Instead Raise Progressive Revenue, and Wealthy Residents Can Afford to Pay More

While state revenue shortfalls are staggering, and it would be best for the federal government to step in with borrowed funds, states can in fact raise revenue to protect state residents and services.

State and local budget shortfalls are enormous as a share of state spending, but significantly smaller when considered as a share of the potential tax base. Below is a table of all the state revenue shortfalls announced to date as a share of 2019 state personal income.

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1 This includes $500 billion in direct grants to states, an increase in the federal Medicaid matching rate, and other targeted supports.

2 See examples in Ohio (Policy Matters Ohio 2020; Schiller 2020); New York (New York Division of the Budget 2020); and California (Fensterwald 2020; California Budget and Policy Center 2020).

TABLE 1. STATE SHORTFALLS ARE LARGE AS SHARE OF STATE REVENUES, BUT MANAGEABLE AS SHARE OF PERSONAL INCOME

State Name	2020 Revenue Shortfall ($ in millions)	% Decline	2021 Revenue Shortfall ($ in millions)	% Decline	Combined 2020 + 2021 Shortfall as a Share of Calendar Year 2019 Personal Income
Alaska	-$612	-10%	-$815	-15%	-3.14%
Arizona	-$864	-8%	-$873	-7%	-0.52%
Arkansas	-$353	-6%	-$206	-3%	-0.41%
California	-$9,700	-7%	-$32,200	-21%	-1.59%
Colorado	-$968	-8%	-$2,642	-20%	-1.02%
Connecticut	-$942	-5%	-$2,229	-11%	-1.12%
Delaware	-$324	-7%	-$200	-4%	-0.99%
District of Columbia	-$722	-9%	-$774	-9%	-2.51%
Hawaii	-$792	-11%	-$1,887	-24%	-3.29%
Illinois	-$2,700	-7%	-$7,400	-19%	-1.35%
Iowa	-$150	-2%	-$360	-4%	-0.31%
Kansas	-$827	-11%	-$446	-6%	-0.82%
Kentucky[a]	-$624	-5%	-$1,101	-17%	-0.88%
Louisiana	-$293	-3%	-$970	-10%	-0.57%
Maryland	-$1,125	-6%	-$2,629	-14%	-0.95%
Massachusetts	-$4,510	-15%	-$7,240	-23%	-2.27%

TABLE 1. STATE SHORTFALLS ARE LARGE AS SHARE OF STATE REVENUES, BUT MANAGEABLE AS SHARE OF PERSONAL INCOME (CONTINUED)

State Name	2020 Revenue Shortfall ($ in millions)	% Decline	2021 Revenue Shortfall ($ in millions)	% Decline	Combined 2020 + 2021 Shortfall as a Share of Calendar Year 2019 Personal Income
Michigan	-$3,233	-13%	-$3,052	-12%	-1.25%
Mississippi	-$864	-14%	-$367	-6%	-1.05%
New Hampshire	-$199	-8%	-$395	-15%	-0.68%
New Jersey	-$2,757	-7%	-$7,346	-18%	-1.60%
New Mexico	-$483	-6%	-$2,399	-30%	-3.12%
North Carolina	-$1,643	-7%	-$2,567	-10%	-0.84%
Oregon[b]	-$630	-6%	-$1,303	-12%	-0.87%
Rhode Island	-$281	-7%	-$516	-12%	-1.33%
South Carolina	-$507	-5%	-$643	-6%	-0.49%
Tennessee	-$654	-5%	-$1,413	-10%	-0.62%
Utah	-$1,439	-18%	-$447	-5%	-1.22%
Vermont[c]	-$48	-3%	-$266	-17%	-0.89%
Washington	-$1,109	-4%	-$3,431	-13%	-0.92%
Wyoming	-$152	-13%	-$280	-25%	-1.18%

Sources: State Budget Shortfalls: Data and sources collected by the Center on Budget and Policy Priorities (CBPP 2020); current as of June 30th, 2020.

Personal Income Data: US Bureau of Economic Analysis, "Table 1. Personal Income, Population, and Per Capita Personal Income, by State and Region, 2018-2019," https://apps.bea.gov/iTable/ iTable.cfm?reqid=70&step=1&isuri=1&acrdn=6#reqid=70&step=1&isuri=1 (accessed June 29, 2020). Note: States with no shortfall data currently available have been omitted.

[a] *FY21 is estimate for just first two quarters.*

[b] *FY22 is estimate for 2021-2023 biennium.*

[c] *FY20 includes $167 million in taxes deferred to FY21, which will be credited to FY20 when collected.*

Some state shortfalls are exceptionally large as a share of the state economy: Alaska, Hawaii, and New Mexico are all facing revenue losses of greater than 3 percent of personal income, and other oil-dependent states may see similar drops. But the typical two-year state revenue drop is approximately 1 percent of 2019 state personal income. Raising this much revenue entirely at the state level requires significant changes to many state tax codes, but it is feasible, preferable to sharp budget cuts, and necessary given that many states chronically underinvest in their residents and employ regressive tax policies that should be reformed.

It is true that income is likely to drop significantly this year and next, but these drops are not uniform; many state residents and businesses would see relatively little direct economic disruption if states protected their workers and services, and they would still be able to afford higher tax contributions.

The June Bureau of Labor Statistics (BLS) jobs report, which reflects survey data collected in mid-May, when the unemployment rate spiked in response to COVID-19 shutdowns, showed that 32.5 million Americans were out of work because of the crisis—19.7 percent of American workers out of a job.[3] The most recent projections from the Congressional Budget Office (CBO) indicate that US GDP for the second quarter (April through June) is likely to reflect an annualized drop of almost 40 percent (Swagel 2020), an unprecedented shrinking of economic activity. But these numbers hide significant differences among households. Many households saw all household workers become completely unemployed or have to dramatically cut back hours due to illness or childcare disruptions, while many other households had no disruption to their income at all.

According to the Census Bureau's emergency Economic Pulse survey, as of the end of May, 48 percent of respondents stated that someone in their household had experienced a loss of employment income since March 13, the day that some US localities began shutting down schools and businesses or issuing stay-at-home orders for residents. Fifty-two percent indicated that they had experienced no such loss. Among the lowest-income households, those earning less than $35,000 per year, 58 percent had lost employment income in the period covered by the survey. Meanwhile, only one in three households earning more than $200,000 per year indicated *any* loss in employment income. While the true unemployment rate spiked higher than at any point during the Great Depression (Jones 2020),[4] more than two-thirds of high-income households lost no employment income at all.

[3] These figures include workers misclassified in the BLS data as either "not at work for other reasons" or "out of the labor force" because of confusion in responses (Shierholz 2020).

[4] The official unemployment rate for April significantly undercounted the unemployed due to a misclassification error.

Losses in employment and income have also been heavily concentrated among workers of color. While 43 percent of white respondents reported a loss in household employment income, that figure is 56 percent for Black respondents and 61 percent for Latinx respondents. Black and Latinx workers, especially women, have been hit incredibly hard by both the pandemic itself and the economic fallout (Gould and Wilson 2020).

The above data focus on job loss and losses of employment income, which have been extremely severe. Yet, interestingly, data from the Bureau of Economic Analysis indicate that total personal income actually *rose* in April, by 10.5 percent (after having fallen by 2.5 percent in March) (Bureau of Economic Analysis 2020). This is likely largely driven by the CARES Act, which provided a $1,200 check to most American households, and a $600-per-week enhancement to unemployment benefits for eligible workers (Yglesias 2020). The federal relief bill did what it was supposed to do, and without it, the situation for families and the economy would be much worse.

It is also important to look past income to wealth, which is even more concentrated. Wealthy families can weather a loss in income or employment without facing economic calamity and can continue to grow richer despite recessions. Upper-income families saw their wealth increase from 2001 to 2016, by 33 percent, while all other families *lost substantial wealth* over the period, never recovering from the Great Recession (Horowitz, Igielnik, and Kochhar 2020).

COVID-19's disproportionate toll on people of color also comes on top of enormous racial wealth disparities, with the typical white family holding 10 times as much wealth as the typical Black family and 7 times the wealth of the typical Latinx family (Solomon and Hamilton 2020). This leads to much lower cash reserves. While average household liquid assets totaled $49,529 for white families in 2016, that figure was only $8,762 for Black families, and the gap persists across education, industry, and homeownership status (Gould and Wilson 2020). The Black-white wealth gap grew starkly during the Great Recession and never returned to prerecession levels (Hanks, Solomon, and Weller 2018).

A just—or even adequate—response to the pandemic *must* ask wealthy, predominantly white households, and those who have not been directly affected by the current crisis, to contribute more, and invest in services and aid for those who need them most (Williams and Sanders 2020).

States Must Also Use This Opportunity to Fix Their Broken Tax Codes

This is also an opportunity for states to fix their upside-down tax codes. According to research by the Institute for Taxation and Economic Policy, 45 states currently have tax structures that *worsen* economic inequality. The vast majority of state tax systems are regressive, with the bottom 20 percent of the income distribution paying, on average, a state and local tax rate more than 50 percent higher than that paid by the top 1 percent. Nationwide, the lowest-income 20 percent of taxpayers pay 11.4 percent in state and local taxes, while the top 1 percent pay only 7.4 percent (Wiehe et al. 2018). Much of this is driven by heavy reliance at the state level on regressive sales and excise taxes, and under-taxing of wealthy residents in states with low taxes and poorly funded schools, health systems, and other services.

These regressive tax policies also exacerbate racial inequity (Hill 2019) and are frequently rooted in historical and present-day racism (Hill et al. 2019) (Leachman et al. 2018).

The shape of the current crisis makes it particularly important, and achievable, for states to fix their broken systems. States that currently over-rely on consumption taxes are unusually hard-hit during this crisis, as sales taxes—especially enhanced sales taxes on restaurants and hospitality—have fallen much more dramatically than income has.[5] And states that already underspend on services are facing large gaps as a share of typical revenue, but have significant room to increase their too-low taxes on their richest residents to close their funding gaps.

[5] Usually broad-based consumption taxes show less volatility in a recession.

Fines and Fees Are NOT the Answer

One kind of "revenue raiser" should be completely off the table during this crisis: increases in civil and criminal fines and fees. Reliance on fines and fees to finance public services is not only regressive; it is directly connected to increases in the over-policing of Black and brown communities (US Commission on Civil Rights 2017) (Kim 2018). The Department of Justice report on the police mistreatment of residents of Ferguson, Missouri—the site of Michael Brown's killing at the hands of police and the subsequent protests in support of Black lives—paints a detailed picture of the injustices perpetrated by city officials when the budget depends on tickets and arrests (US DOJ Civil Rights Division 2015). In that jurisdiction and fiscal year, the city funded 25 percent of its budget through fines and fees, issuing a staggering 90,000 citations and summonses in a city with only 21,000 residents. Ninety-three percent of those cited were Black (US DOJ Civil Rights Division 2015).

Additionally, because fines and fees take no account of ability to pay, huge portions of the resulting revenue are spent directly on attempting to collect debts (Menendez et al. 2019), and imprisonment for failure to pay such debts is a significant driver of incarceration in many places (Council of Economic Advisers 2015). This dynamic is playing out even now, as courts continue to attempt to collect fees despite the closure of the court system due to the pandemic (Hager 2020).

These policies are suffused with racism from inception. Research has shown that the willingness of local officials to rely heavily on fines and fees is closely correlated with the proportion of the policed populace that is Black, and negatively correlated with Black representation in elected office (Sances and You 2017).

Increasing Taxes and Spending Is Good for State Residents and Economies

State and local government budgets are composed of some of the most visible and important government services provided to most American families. The two largest expenditures in most state budgets are health care (largely through the Medicaid program) and education.[6] And these are exactly the public goods now on the chopping block.

State lawmakers across the country are proposing Medicaid cuts, despite the fact that Medicaid funding is generously matched by the federal government (Roubein and Goldberg 2020). Public schools had laid off more than 750,000 K—12 education employees by mid-May when schools were still in session (Gould 2020a). Public K—12 education employment never recovered after the Great Recession—despite growing school enrollment—and is now significantly lower than its lowest point during that downturn (Gould 2020b).

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[6] Note that different states distribute education funding at the local level through different mechanisms.

States and localities are also responsible for public health departments, the maintenance of critical infrastructure like drinking water and wastewater systems, and transit systems and other forms of local transportation. And they administer the programs vulnerable families rely on in times of crisis, including Temporary Assistance for Needy Families (TANF), the Supplemental Nutrition Assistance Program (SNAP, also known as food stamps), Unemployment Insurance (UI), home nutrition for the elderly, child and family services, home visiting programs, and many more. Some states also provide cash assistance to the poor, though these important expenditures make up less than 1 percent of state budgets (CBPP 2018).

All of these services are important in their own right and worth funding for the many benefits they bring to residents, but they serve an additional function in macroeconomic downturns: stimulating demand for goods and services and supporting economic recovery.

Economists measure the bang-for-the-buck of fiscal stimulus using "multipliers." If a policy has a multiplier of 1.5, it creates $1.50 of economic activity for every $1 spent by the government. If the multiplier is 0.5, then the policy only creates 50 cents of economic activity per $1 spent. The multiplier for a policy depends on how much of the money is spent immediately (versus put into savings), whom it goes to, and how much it continues to circulate; the more a program is targeted toward direct purchases and job creation, or transfers to households in immediate need of cash, the higher the multiplier will be.

The CBO has estimated the multipliers associated with various provisions of the American Recovery and Reinvestment Act of 2009 (the 2009 Stimulus) (CBO 2015). According to their estimates:

- Direct government purchases of goods and services created between 50 cents and $2.50 of economic value for every $1 spent[7] (average $1.50);
- Transfer payments to low-income and unemployed individuals created between 40 cents and $2.10 of value for every $1 spent (average $1.25);
- Two-year tax cuts for low- and moderate-income households created between 30 cents and $1.50 of economic value for every $1 spent (average 90 cents); and
- One-year tax cuts for higher-income households created between 10 cents and 60 cents of value for every $1 spent[8] (average 35 cents).

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[7] I cite here the multiplier for "purchases of goods and services by the federal government." The CBO also offers separate multipliers of 2.2 and 1.8, respectively, for transfers to states and localities for infrastructure and transfers for other purposes, but these are primarily lower due to the likelihood that some of that money replaces borrowing or spending down of reserves, and thus there is not a dollar-for-dollar increase in state spending.

[8] Note that this was the increase in the exemption to the alternative minimum tax (AMT), which at the time was seen as hitting many "middle class" families as well as the rich.

The best stimulus policy is clear: Pour money not into tax cuts but into direct purchases of goods and services by the government and transfers to low-income and unemployed people. Conservatively, using the average of the low and high multiplier estimates from the CBO, it would take $4.29 in higher-income tax cuts to equal the $1.50 in stimulus created by $1 of direct expenditures. Payments to those who truly need them, like unemployment insurance and refundable tax-credits for low-income residents, are 3.6 times as valuable as tax cuts for the wealthy.

For state policymakers dealing with yawning deficits they can't finance with borrowing, the inverse is equally clear: Tax increases, especially those that fall on the rich, are far less damaging than spending cuts. In fact, not only should spending not be cut to avoid a tax increase, further increasing taxes on the rich in order to *increase* spending would provide a large boost to the local economy. Raising an additional dollar of revenue from a high-income person during a recession, using the same conservative mid-range multipliers as above, would only reduce economic output by 35 cents. When that dollar is then spent on government services, it conservatively creates $1.50 of new economic activity, for a *net* economic surplus of $1.15 per dollar of revenue raised and spent. Using the high end of the CBO's multiplier estimates, which would be consistent with recent research (Blanchard and Leigh 2013) (Chodorow-Reich et al. 2012), yields a *net* multiplier for spending financed by taxes on the rich of 1.9.

Tax increases, especially those that fall on the rich, are far less damaging than spending cuts. In fact, not only should spending not be cut to avoid a tax increase, further increasing taxes on the rich in order to increase spending would provide a large boost to the local economy.

This effect was well-known by the time of the Great Recession (Johnson 2010), and many states did raise some new revenues during that period (Johnson, Collins, and Singham 2010), but they also relied heavily on spending cuts to balance their budgets, especially when critical federal aid expired too early. States that cut government employment most dramatically saw the slowest economic recoveries and the deepest job losses, including when only private-sector job losses are counted, as cuts rippled through local economies and depressed economic activity (Cooper 2020).

These estimates focus only on total short-term economic activity, not the social benefit or long-run economic benefit of government spending. Cutting SNAP or UI benefits doesn't just reduce grocery sales and income to farmers and cashiers; it forces children to go hungry. Laying off a teacher does more than reduce her consumer spending; it damages her students and their long-term productivity (Johnson 2020). Meanwhile, tax cuts for the rich and corporations are ineffective stimulus, exacerbating income inequality and harming our democracy (Saez and Zucman 2020).

States Should Use Automatic Tax Increases, Not Spending Cuts, to Insure against Federal Inaction or a Worsening Economy

Many states and localities have very limited legislative sessions, and they entrust executives with the power to freeze or cut spending, but not change tax law. This biases state responses to revenue shortfalls. Gov. Gavin Newsom (D-CA) has gone a step further, by partly relying on assumed federal aid to backstop his revised budget proposal, while building in another $14 billion in automatic spending cuts if the HEROES Act state and local fiscal relief package does not pass.

Automatic spending cuts should be replaced with automatic tax increases focused on the wealthy.[9] One approach to automaticity in the current crisis would be to increase taxes by more than is necessary to fill current shortfalls and enact automatic tax reductions that can be triggered in case revenues come in *higher* than expected. There is no reason that states must default to service cuts simply because the legislature is not in session, when tax responses are far preferable economically.

9 Tax law scholar David Gamage argued during the last recession that states should automatically raise taxes in times of recession and cut them in times of expansion because spending volatility is significantly more damaging than revenue volatility (Gamage 2010).

State Budget Cuts Cost the Economy Millions of Jobs in the Great Recession

State and local government austerity has the power to turn the current economic downturn into a long, grinding depression nationwide—just as it deepened and prolonged the Great Recession.

According to the Center on Budget and Policy Priorities, state budget shortfalls from fiscal year 2009 through fiscal year 2013 totaled $600 billion (McNichol, Leachman, and Marshall 2020). The cuts made to close these shortfalls—which are significantly smaller than the shortfalls states and localities are now facing (Bartik 2020)—have had a lasting impact on the US economy. Had state and local spending recovered consistent with historical precedent, it would have been *$800 billion higher* in 2013, supporting an additional 8 million jobs, for an unemployment rate of 4.4 percent. Instead, state and local spending cuts delayed America's return to pre-crisis unemployment levels by four years, to 2017 (Bivens 2020). We must not make the same mistake now. If the federal government does not provide more fiscal relief, or if the funding proves inadequate, revenue increases should be the first line of defense against deficits, not layoffs for teachers and health care workers or cuts to services.

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PROGRESSIVE TAX PROPOSALS FOR INCREASING STATE AND LOCAL REVENUE

Tax changes can help states close their budget shortfalls while protecting vulnerable communities and state economies. States and localities have a number of options for increasing revenues in a progressive way, right now.

Enhance Income Taxes

One simple way for many states and localities to raise progressive revenue quickly is to increase their income taxes, which can be targeted to high earners, who are both most able to afford the payments and least likely to spend any marginal dollar. Progressive income taxes can also be responsive in real time to changes in a household's situation, such as a lost job, through wage withholding.

Forty-two states, and some larger municipalities, have income taxes, but in many places, income taxes are low and insufficiently progressive. Nineteen states with income taxes have no brackets starting above $20,000. Twenty-seven have no additional gradations above $100,000 (Grundman and Wiehe 2020). Increasing rates and adding extra brackets is quite simple. Some states have legal prohibitions on progressive rate structures, but progressivity can be achieved through targeted credits at the low end and limits on deductions and exemptions at the high end.[10] Many states have room to raise more income tax revenue by closing down specific loopholes or ensuring that more income is taxed (C. Davis 2020).

States should look toward millionaire's tax proposals—and those with extreme inequality like New York are already considering additional taxes at even higher levels (Fiscal Policy Institute 2019)—but it is not only millionaires who can afford to pay more in state taxes. States should comprehensively reexamine their income tax rates, brackets, and loopholes to ensure progressivity at every level, and should look to tax increases before service cuts even if some of those taxes fall on families outside the very rich.

Policymakers can also increase tax progressivity and shield lower-income households from other taxes (like property taxes, which can be difficult to target) by adding or enhancing state earned income tax credits and other refundable credits within state income taxes. This is much more efficient than creating large carve-outs that benefit the rich as much as they do the residents they were supposed to help.

Recapture Federal Giveaways to the Rich

America's most fortunate households and largest corporations have recently been the beneficiaries of trillions of dollars of deeply unpopular federal tax cuts, via the 2017 Tax Cuts and Jobs Act (TCJA). Raising taxes at the state and local levels to recoup this lost revenue would significantly bolster state and local budgets while leaving wealthy state residents no worse off than if the TCJA had never been passed (Richards 2018a).

First, many states "couple" portions of their tax codes to the federal code for ease of administration, in ways that have directly reduced state taxes since the TCJA. States that have an estate tax—an extremely progressive revenue source—coupled to the federal rules saw revenues decline dramatically when the TCJA doubled the exemption for the federal

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[10] For more on state income taxes, see the Institute for Taxation and Economic Policy's recent analysis (Grundman and Wiehe 2020).

tax (Richards 2018b). Similarly, states should decouple from the TCJA's "pass-through deduction" (199A) if they have not, and in fact consider increasing taxes on such income to capture the windfall the provision created ("Project SAFE" 2020). There are a host of ways that states could claw back lost revenue, and more, by strategically decoupling from federal tax rules (Shanske 2019), including new corporate tax giveaways in the CARES Act.

One provision of the TCJA that raised revenue from the rich was the so-called "SALT cap," which limited the total amount of state and local taxes that can be deducted from federal taxable income to $10,000. The HEROES Act currently includes a two-year repeal of this provision, which would funnel $136 billion to the richest households in these states (Ziv 2020). This is a mistake that will waste revenue and increase inequality, not help state budgets. If the SALT cap is repealed, states should move quickly to capture that money for state budgets, and to further raise taxes on their wealthiest residents, knowing that top-bracket payers will get 37 percent of any additional state taxes back on their federal return.

States can attack these federal giveaways directly, or simply raise income taxes on high-income households knowing that these households will still pay lower total rates than they did just a few years ago, before the TCJA. A state wishing to recapture some of the corporate tax giveaways in the TCJA could enhance its own taxation of capital income, or even financial wealth, to directly tax their residents' share of corporate windfalls. Federal income tax giveaways could be targeted with enhanced taxes on the specific activity in question, with the rates set to recoup the full value of the federal giveaway, essentially taxing the taxpayer as though the giveaway didn't exist. For example, states can tax capital gains income at *higher* rates than labor income to claw back the special low rates on capital gains at the federal level.

Raise Corporate Revenues

Corporate income taxes are extremely progressive, with between a third and half of corporate taxes being paid by the top 1 percent of households (Huang and Debot 2017). Further, corporate taxes in any given year are only paid by profitable corporations, so increased corporate taxes will not harm businesses that have been hardest-hit by the COVID-19 crisis.

The TCJA slashed the top corporate tax rate from 35 percent to 21 percent and cut federal corporate revenues by an estimated $750 billion over 10 years (Hendricks and Hanlon 2019). This creates plenty of room for states to increase their own corporate tax rates to recoup this revenue, especially as many states have cut their corporate tax rates recently.

States should also decouple from some of the CARES Act's corporate tax provisions (Thimmesch 2020), which lose revenue, and consider *conforming* to certain revenue-raising aspects of the TCJA (Shanske 2020) (Shanske and Gamage 2019) (Shanske and Gamage 2018).

States could enact something akin to the Real Corporate Profits Tax, initially proposed at the federal level by Sen. Elizabeth Warren's presidential campaign (Yglesias 2019). This tax acts as a surcharge to complement existing corporate taxes, but the rate is applied to corporate profits as they are reported *to investors* rather than profits as they are reported to tax authorities. These two numbers can be very different, and a number of extremely profitable corporations escape corporate income taxes entirely.

States could even consider enacting state-level excess profit taxes, designed to discourage profiteering and recapture windfalls earned by companies that happened to be well-positioned to benefit from the pandemic. One way to approach this would be an additional, potentially quite high, tax rate on any profits in excess of the average profits earned by the corporation in the prior three years (Avi-Yonah 2020).

Reform Wealth Taxation

Darien Shanske and David Gamage have recently offered two promising ideas for states looking to fund services by taxing wealth (Gamage and Shanske 2020). While the authors would ideally levy a one-time comprehensive wealth tax like that advocated at the federal level by legal scholar Daniel Markovits (Markovits 2020), they recognize the administrative difficulty for state governments in creating an entirely new tax and system of asset valuation to respond to this crisis. Instead, they propose either a statewide real property tax with a large exemption (piggybacking on local property tax assessments) or a "deemed realization" in which as-yet-untaxed capital gains are immediately included as income for state income tax purposes, which would get around some states' prohibitions on general wealth taxes but create some significant administrative puzzles. These are very interesting contributions that are worth serious consideration, especially by states with the ability to create payment plans or loan programs and issue revenue bonds, to bring in immediate revenue while allowing residents to smooth their payments over a number of years.

For localities, property taxes are an obvious source of increased revenue, though because many homeowners will be unable to pay large new tax bills that are not based on income, they can be coupled with refundable income tax credits to offset property tax increases for both homeowners and renters ("Project SAFE" 2020b). States should also enact or increase estate or inheritance taxes, which are an extremely progressive revenue source (McNichol 2016).

Modernize Consumption Taxes

The current crisis has led to unprecedented declines in sales tax revenues, especially from restaurants and travel-related expenditures. Sales and excise taxes are generally quite regressive, with households at the bottom paying on average 7.1 percent of their income in state and local sales and excise taxes, while those in the top 1 percent pay only 0.9 percent (Wiehe et al. 2018). There are many ways, however, that states can make their consumption taxes both more robust and more progressive, by reforming what is taxed to include more services (legal and professional services, gym memberships, spa treatments, etc.) and to ensure that taxes are collected on online purchases.[11]

CONCLUSION

States must move now to protect their residents and economies.

While it is imperative that the federal government enact broad state and local fiscal relief, state policymakers must also act now to invest in their residents, bolster their economies, and push back against skyrocketing inequality. The needs created by this crisis, and by chronic underinvestment in health, education, housing, and human services, will require states to go beyond their previous budgets. This will require significant new revenue, but states have many ways to raise this revenue while protecting low-income individuals and families. This is the only path toward a just recovery, and the consequences of cutting jobs and services instead will be dire.

[11] See (C. Davis 2019), (Escoto 2020), and (A. Davis 2020).

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ABOUT THE AUTHOR

Kitty Richards is a freelance policy consultant and strategic advisor to the Groundwork Collaborative. She has previously worked on federal budget and tax policy at several think tanks, including the Center on Budget and Policy Priorities and the Center for American Progress, and has served as an economic policy staffer on Capitol Hill and in the White House. She also spent several years working on local issues, as chief of staff to DC Councilmember Elissa Silverman and as acting executive director of the DC Fiscal Policy Institute, managing staff and working on a wide range of issues including tax and budget policy, workforce policy, housing and homelessness, and paid leave. She contributed to the enactment and implementation of the Universal Paid Leave Act, passed in 2016, which established a social insurance fund for paid family and medical leave for DC workers. The fund began paying benefits in July 2020.

Kitty received her bachelor's degree in biochemistry and molecular biology from Reed College, and her JD from the New York University School of Law, as part of the Leadership Program in Tax Law and Fiscal Policy.

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