

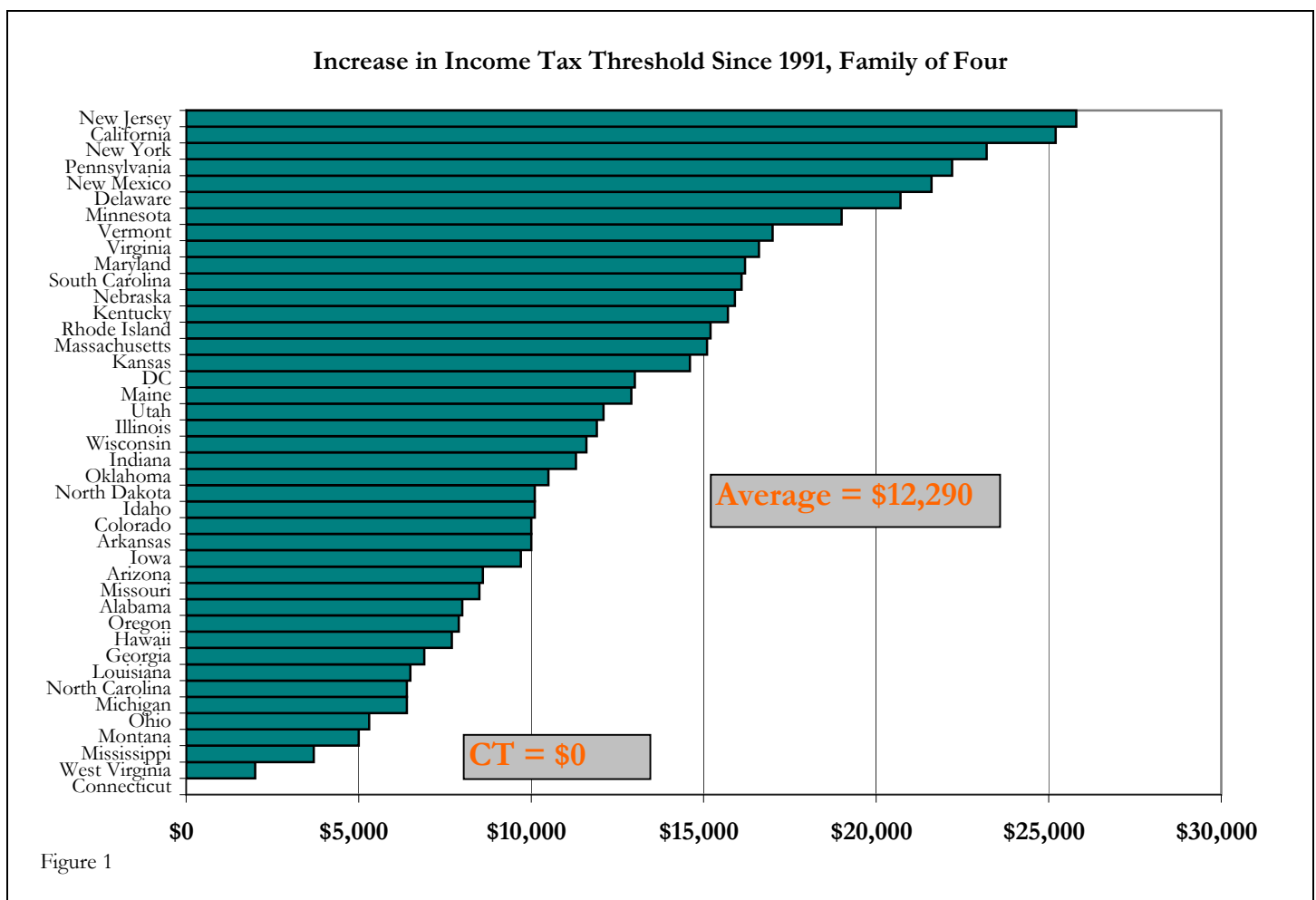


Connecticut Families Hit By Outdated State Income Tax Threshold

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Connecticut's tax threshold has been frozen for over 16 years.¹ The "tax threshold" is defined as the income level at which a taxpayer first owes income tax, taking into account exemptions, credits and deductions that are *universally* available. Connecticut's tax threshold for families has not been increased since the enactment of the personal income tax in 1991. This means that each year, an increasing number of low-wage families are becoming subject to the state's income tax. A family of four earning just \$24,100 can owe the state some income tax.² Connecticut is the **only state in the nation** with an income tax that has not adjusted its tax threshold upward since 1991. Over this period, the average amount by which states have increased their tax thresholds for a family of four is \$12,290, as seen in Figure 1 below.



Compared to the federal poverty level, Connecticut's tax threshold has plunged in the past 17 years. In 1991, Connecticut's tax threshold was 73% higher than the federal poverty line. Since the state has not moved its threshold and the federal poverty line increases annually with inflation, our threshold today is just 14% over the federal poverty line. This 59 percentage point drop is by far the largest in the nation. It stands in stark contrast to national averages, where the tax threshold has increased by 29% relative to the federal poverty line. The federal poverty line has increased by 52% since 1991. Figure 2 below shows the erosion of the gap between Connecticut's income tax threshold and the federal poverty threshold. Without legislative action, Connecticut will soon be requiring families with poverty-level incomes to pay the state income tax.

If Connecticut's threshold were the same amount above the federal poverty line as in 1991, the tax threshold today would be \$38,713. Our income tax threshold has fallen well below where it was originally placed 17 years ago.

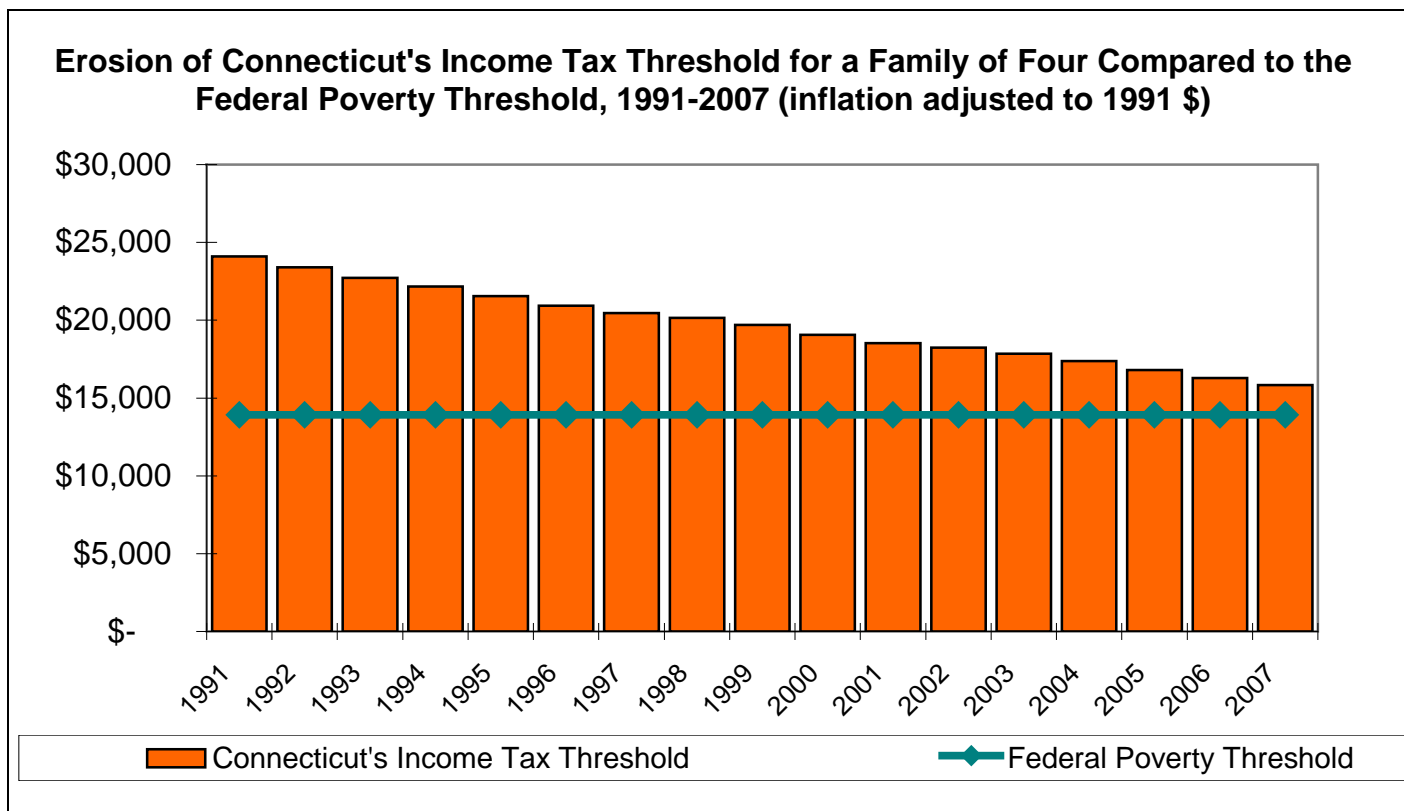


Figure 2

Connecticut, once a leader in appropriately targeting the income tax, now stands by as other states create more supportive conditions for low-wage working families. When Connecticut's income tax was enacted, the state provided the highest threshold in the nation. This is no longer the case. In 1997, two states had a higher threshold. By 2007, 22 states and Washington D.C. had higher thresholds, and Connecticut's tax threshold for a family of four stood just \$100 above the national average, and only 52% of California's nation-leading threshold of \$46,100. Moreover, Connecticut's income tax threshold is the lowest in the region, below every New England state with an income tax, as well as neighboring New York and New Jersey. Figure 2, above, vividly shows how Connecticut has fallen behind since 1991.

The overall regressivity of Connecticut's tax system could be reduced with a higher tax threshold. Poorer families spend a higher percentage of their incomes on state and local taxes than do high-income earners. The Connecticut General Assembly's Program Review and Investigations Committee noted that Connecticut's personal

income tax “does not offset the regressivity of the state’s sales, excise and property taxes.” Increasing the tax threshold would make our tax system more fair.

Other changes to the income tax could make it more equitable. A refundable state earned income tax credit (EITC) would benefit our low-wage families; Connecticut is the only New England state with an income tax that does not also have a state EITC. Increasing income tax rates for higher income earners would also make the system fairer. Our wealthiest 1% of taxpayers (with average income of \$3.3 million) in 2006 paid just 4.7% of their income in state and local taxes (taking into account federal income tax deductions), compared to the 10.2% of middle-income of taxpayers (middle quintile, average income of \$55,100) and 10.9% of the income of our low-income families (low quintile, average income \$15,100).³

Changes to Connecticut’s income tax should be part of a larger effort to overhaul Connecticut’s state and local tax system. Increasing Connecticut’s income tax threshold and instituting a state level earned income tax credit would make Connecticut’s income tax system more fair, as would instituting a progressive income tax increase on Connecticut’s top income earners. While *fairness* is an important attribute for an overall tax system, at least as important is *adequacy*. As Connecticut faces dire projections of budget deficits, addressing the shortcomings of Connecticut’s income tax system may be necessary to meet the needs of Connecticut’s communities and families. Moreover, increasing state income tax revenues through a modest increase in the tax rates paid by Connecticut’s wealthy families would enable the state to increase its share of education financing, thereby giving middle-income families a much-needed break on their property tax bills.

¹ This brief relies on a recent analysis by the Center on Budget and Policy Priorities. (Jason A. Levitis and Andrew C. Nicholas, “The Impact of State Income Taxes on Low-Income Families in 2007.”)

² For example, since some, but not all, families are eligible for the property tax credit against the income tax, this credit is not included when calculating the tax threshold. For families who are able to claim the credit, the point at which they are liable for income taxes is obviously higher.

³ Institute on Taxation and Economic Policy, *Who Pays?*, 3rd edition (forthcoming, 2008).