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In cross-border competition, Lamont's tax cut plan offers CT a win

By Greg Bordonaro
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For more than a decade, Connecticut has gotten beat up in the national press — particularly in the Wall Street Journal's editorial pages — for raising taxes amid continued budget instability.

Conversely, our neighbor to the north over the years shed its "Taxachusetts" image by cutting some taxes and installing new restrictions that limit property tax growth.

Since the Great Recession of 2008, Massachusetts' economic and job growth have far outpaced Connecticut's. LEGO's recent decision to relocate from its 50-year-old U.S. headquarters in Enfield to Boston served as another Bay State victory.

Cross-border employment trends
CONNECTICUT VS. MASSACHUSETTS

	Connecticut	Massachusetts
2008 Peak employment	1.72M jobs (March 2008)	3.33M jobs (April 2008)
Dec. 2022 employment	1.67M jobs	3.73M jobs
Change in employment	-53,000	401,600
% Change	-3.1%	12.1%

Source: Economist Don Klepper-Smith

But Connecticut now has an opening to improve its standing in this cross-border competition.

Gov. Ned Lamont earlier this month unveiled one of the largest tax cuts in Connecticut history, including reducing the income tax for middle-class earners.

His two-year, $50.5 billion budget also includes tax relief for small businesses and low-wage workers.

This follows a $600-million tax cut approved by lawmakers last year, amid the state's newfound budget stability brought on by strong stock market returns during most of the pandemic and federal stimulus funding.

Just as important: Lamont and legislative leaders have agreed to extend for 10 years key budget and spending controls adopted in 2017 that have also contributed to recent surpluses.

In contrast, Massachusetts voters in November approved by referendum a significant income tax hike on their state's highest earners. Bay State voters approved adding a 4% surtax to Massachusetts' flat 5% income tax rate on individuals earning more than $1 million.

That puts Massachusetts' top income tax rate at 9%, above Connecticut's top 6.99% tax bracket for single filers who earn more than $500,000, or joint filers who earn more than $1 million.

Massachusetts voters approved the millionaires tax hike — which is expected to raise $1.3 billion annually, according to Tufts University — despite their state enjoying a budget surplus. The tax hike also comes as Massachusetts loses population at faster rate than Connecticut.

So, what's this all mean? Will Massachusetts' millionaires suddenly flock to Connecticut's shores?

No, that's not the point of this column. I wouldn't expect that to be a trend. If Massachusetts' millionaires are fed up with paying higher income taxes they are more likely to relocate to southern, low-tax states than Connecticut.

However, any steps Connecticut takes to improve its competitiveness with a Northeast neighbor is a good thing, particularly following what some consider a lost last decade for the state in terms of economic and job growth.

We also have an opportunity to create some positive headlines nationwide — a rare change from recent history. That might encourage some businesses and residents to give Connecticut that "second look" Gov. Lamont has talked about in the pandemic's wake.

Lamont's tax cut plan remains only a proposal. Lawmakers still need to approve it, and there are some in the legislature who are still pursuing tax hikes despite the state's budget surplus and plush rainy day fund.

For example, Senate Pro Tempore Martin Looney (D-New Haven) is once again pitching his mansion tax that would increase taxes on homes valued at over $2 million.

Those types of proposals, even if they don't pass, aren't helpful.

Why don't we want to scare off the state's top earners?

As much as we talk about tax inequality in this state and country, the reality is the state's wealthiest residents foot the bill for a significant portion of the state budget. The state's top 2% of tax filers paid 40% of the state income tax in 2020, the Hartford Courant recently reported, while the bottom 54% of filers paid 4% of the income tax.

Wealthier residents also have an easier time relocating to other lower-tax states.

Taxes aren't everything

Of course, it's important to put tax policy in perspective in terms of the impact it has on where individuals choose to live or operate a business.

Joseph Feehan

It’s only one of many factors companies take into consideration, said Joe Feehan, a state and local tax partner in the Boston office of accounting and consulting firm Marcum.

We know this well in Connecticut following the recent or pending departures of three company headquarters to Boston.

Top executives from all three companies — General Electric, Alexion and LEGO — cited a desire to be in a more vibrant urban center that attracts top talent. They didn’t mention taxes as a deciding or even significant factor in their moves.

We know that Connecticut’s lack of a destination city puts the state at a disadvantage to Massachusetts and New York, which are our top competitors in terms of business attraction and retention, Feehan said.

New York City and Boston also have stickier industry clusters.

“I think to a large extent, financial services will always be in Manhattan,” Feehan said. “And I think for Boston, pharma, life sciences, even if those types of companies wanted to leave, they kind of need to be there for non-tax reasons.”

Economist Don Klepper-Smith, a longtime critic of Connecticut’s economic and tax policies, said Massachusetts has had a stronger economic development strategy over the years focused more on maximizing economic growth and supporting employers.

Connecticut, at times, has taken the opposite approach; jobs-growth data reflects the two states’ diverging paths, he said.

From their peak job levels in 2008, when the Great Recession wreaked financial havoc globally, Connecticut has lost 53,000 jobs (a 3.1% decline), while Massachusetts has gained over 401,000 jobs (a 12.5% increase).

Klepper-Smith did say that Lamont's proposed tax cuts are a "step in the right direction," as long as they can be maintained long term.

Lamont, a Democrat, does seem to be a more fiscal conservative, pro-business governor, even though the private sector hasn't agreed with all of his policies (e.g., paid family and medical leave.)

Regardless, tax policy does matter.

Since Massachusetts voters approved the income tax hike, Feehan said he's gotten "a lot of calls" from wealthy individuals and business owners who are asking about changing their residency.

Of course, that's easier said than done, particularly for those who still own a business in Massachusetts.

Overall, Feehan said, Massachusetts and Connecticut have a lot of similarities in their tax structures.

And he agreed with my assessment that the Massachusetts income tax hike most likely won't "lead to a bunch of people leaving."

But for a state long-suffering from self-esteem issues, Connecticut should take victories when it gets them, no matter how small.

Lawmakers should approve Lamont’s tax cut plan, while maintaining a focus on long-term budget stability.