MA Raised Revenue in Last 3 Recessions, Reducing Cuts

By Kurt Wise, Senior Policy Analyst

While many states, including Massachusetts, are now beginning a cautious reopening of parts of their economies, the economic impact from the COVID-19 pandemic is likely to be severe and long-lasting. Not only are many families and businesses facing serious financial challenges, state governments are set to see tax collection shortfalls deeper than those of the Great Recession. As of early June, Massachusetts' fiscal year (FY) 2020 tax collections are running more than $2 billion behind expectations. For the coming fiscal year (FY 2021), the tax shortfall could exceed $7 billion.

Snapshot of Findings

- During each of the last three recessions, MA lawmakers raised revenue, delayed planned tax reductions, and/or reduced tax breaks for corporations.
- The size of the annual revenue gains from these changes ranges from $1.1 billion to $2.5 billion (in 2020 $s).
- By delivering additional revenue, these increases helped prevent or reduce budgets cuts that otherwise would have been necessary to achieve balance.
- Raising additional revenue from high-income households and profitable corporations is better for economic recovery than are budget cuts.
- Cutting budgets and failing to invest in communities hardest hit by the pandemic perpetuates the deep racial inequities built into the current system.

Fortunately, Massachusetts has a variety of resources and options for addressing this shortfall. Resorting to cuts will slow our state's recovery and further harm communities hit hardest by the convergence of racist policies and the global pandemic. The federal government has directed some $2.5 billion in aid toward the Commonwealth thus far (though it is unclear how much of this will be available to help address the state's budget shortfall), and there remains hope that billions more could be forthcoming in the months ahead. State lawmakers also have built up a $3.5 billion reserve in our state's Rainy Day Fund.

Still, given the scale of anticipated revenue losses and the likelihood that it will be years before the Commonwealth returns to pre-recession collection levels, it will be necessary for Massachusetts to generate additional revenue if we are to avoid deep, damaging, and unjust budget cuts.

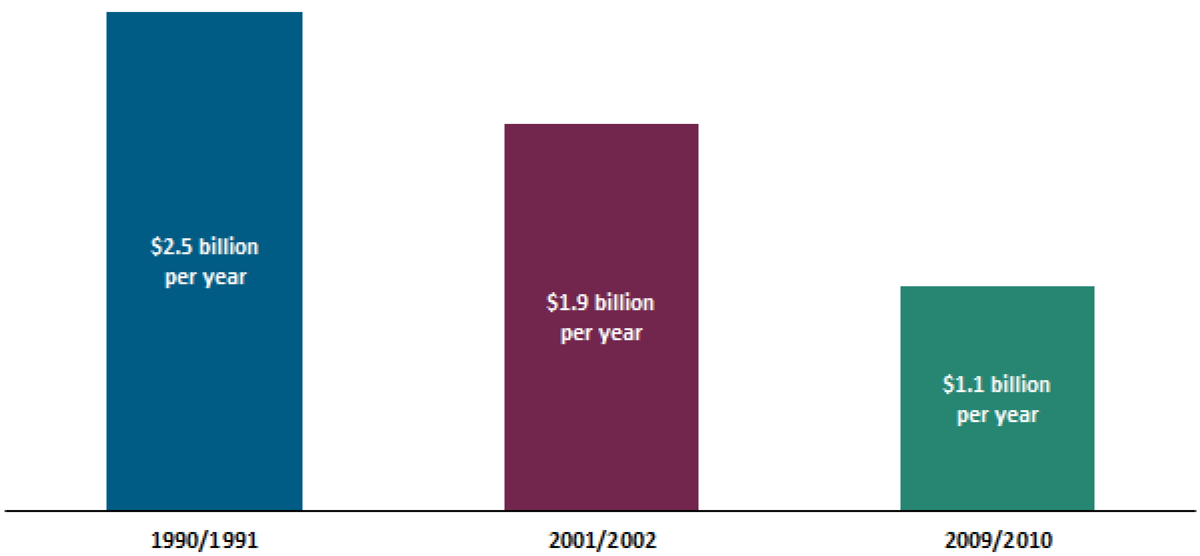
As a respected group of some 100 Massachusetts economists have explained, raising needed revenue from profitable corporations and high-income households will be far better for our state economy than making budget cuts. Evidence from the Great Recession shows that states that maintained their core state and local functions – keeping teachers, firefighters, nurses and other critical service providers on the job – fared better during that recession and saw their economies grow more quickly once the recovery took hold.

Protecting state finances with progressive revenue increases also is central to addressing the racial disparities of the pandemic's impacts. The COVID-19 pandemic has hit communities of color hardest, both health-wise and in economic terms. Our state response must make it a top priority to lay the groundwork for a robust *and* equitable recovery – one that helps dismantle the deep inequalities the pandemic has laid bare. To do this, lawmakers will need to move forward with long-overdue investments – in our students, our workers and our infrastructure. These investments will require collecting additional revenue from those well-positioned to pay something closer to their fair share: profitable corporations and high-income households.

This would not be the first time that Massachusetts lawmakers have chosen to raise additional revenue to address recession-driven shortfalls. In fact, they have done so in each of the last three recessions. Annual revenue gains from the various recession-related changes ranged from $1.1 billion in 2010 to $2.5 billion in 1991 (adjusted for inflation to 2020 dollars).

To help balance the state budget, MA lawmakers have raised revenue in each of the last three recessions

Combined annual revenue increases (in 2020 $s) from recession-related tax law changes, by period of major changes*



Sources: Annual Statutory Basis Financial Reports and Commonwealth General Obligation Bond Official Statements

*See end of factsheet for list of major tax changes

In each case, legislators made a variety of changes to the state tax code. Some of these changes were regressive, meaning lower-income households paid a larger share of their household income toward these tax changes than high-income households did. Such changes included extending the sales tax to more items and raising the sales tax rate, raising gas taxes, and raising cigarette and related taxes.

Other changes were progressive, meaning that lower-income households paid a *smaller* share of their income toward these taxes than high-income households did. These changes included raising tax rates on wage and salary income and delaying planned income tax reductions. Some progressive changes focused more narrowly on high-income households and thus were especially progressive. These included increasing the tax rate applied to capital gains income and dividend and interest income, and decoupling from revenue-losing changes to federal estate tax laws. Notably, legislators also chose at times to decouple from federal corporate tax breaks, thus preventing losses from the state's corporate tax collections (another progressive change).

In short, when faced in past decades with recession-driven revenue shortfalls, Massachusetts lawmakers consistently have made the economically advantageous choice to raise more revenue. *Not* to do so now would be a departure from a long history of choosing revenue increases over budget cuts. Failing to raise additional revenue now likewise would perpetuate, rather than help to reverse, inequalities in our society that disproportionally harm communities of color and households with lower incomes.

Major Tax Changes, by Recession

2009/2010 [1]

- Increased sales tax rate from 5 percent to 6.25 percent
- Established direct broadcast satellite service excise tax
- Increased local option room occupancy excise from 4 percent to 6 percent
- Established local option meals excise of 0.75 percent

2001/2002 [2]

- Suspended scheduled decrease in personal income tax rate from 5.3 percent to 5.0 percent and established benchmarks for later, phased reduction
- Reduced personal exemption from $4,400 to $3,300, with phased return to prior level
- Suspended the charitable deduction
- Increased long-term capital gains tax rate to match the rate for wage and salary income
- Disallowed federal bonus depreciation deduction
- Increased cigarette excise tax
- Amended the state estate tax to avoid reductions due to federal changes

1990/1991 [3]

- Raised personal income tax rate from 5.75 percent to 6.25 percent (for 1991) and 5.95 percent (for 1992)
- Increased the effective rate on long-term capital gains from 5.0 percent to 6.0 percent
- Increased the effective rate on other unearned income (short-term capital gains, dividends, and interest) to 12.0 percent
- Extended sales tax to most nonresidential electricity and gas purchases and to telecommunications services

- Raised gas tax from 11 cents to 17 cents (1991) and to 21 cents (1992)

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[1] See General Obligation Bond Official Statement 12-1-2009, pg. A-6: https://www.massbondholder.com/sites/default/files/downloads/12-1-09%20%24956MM%20GOB%20CL%202009%20SerE%20%28FT%20BAB-DPI%29.pdf
See 2010 Statutory Financial Basis Report, pg. 2: http://www.macomptroller.info/comptroller/docs/reports-audits/sbfr/2010-sbfr.pdf

[2] See General Obligation Bond Official Statement 8-21-2002, pg. A-4 https://www.massbondholder.com/sites/default/files/downloads/8-21-02%20%24670.745MM%20GOB%20CL%202002%20SerD.pdf
See General Obligation Bond Official Statement 11-22-2002, page A-1 https://www.massbondholder.com/sites/default/files/downloads/11-22-02%20%24734.350MM%20GOB%20CL%202002%20SerE.pdf
See Acts of 2002, Ch. 186: https://malegislature.gov/Laws/SessionLaws/Acts/2002/Chapter186
See 2002 Statutory Financial Basis Report, pg. 2-3: http://www.macomptroller.info/comptroller/docs/reports-audits/sbfr/2002/sbfr-2002.pdf
See Massachusetts Department of Revenue Technical Information Release (TIR 02-11): https://www.mass.gov/technical-information-release/tir-02-11-effect-of-federal-bonus-depreciation-allowance-as-revised

[3] See General Obligation Bond Official Statement 2-26-1993, pg. A-15 thru A-17, A-23 thru A-25: https://www.massbondholder.com/sites/default/files/downloads/2-26-93%20%24899.390MM%20GO%20RB%201993%20SerA.pdf