Fair Share Tax on Incomes Over $1 Million Would Generate at Least $2 Billion a Year

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MassBudget estimates that the Fair Share tax on incomes over $1 million is likely to generate at least $2 billion a year in new revenue if approved by voters in November 2022. MassBudget assessed revenue estimates from three respected sources and considered important data differences and assumptions built into each of the three analyses. The following offers a brief overview of each analysis, along with MassBudget's conclusion.

Key Takeaways

- MassBudget pegs the likely revenue gain from the Fair Share surtax on taxable income over $1 million at more than $2 billion per year.
- Massbudget looked at three analyses with estimates ranging from $2.1 billion to $2.7 billion per year.
- "Dynamic factors" that might affect collection totals are likely to have only a modest impact.
- None of the estimates account for revenue gains resulting from new state investments funded by Fair Share.

The Massachusetts Department of Revenue (DOR) estimated that Fair Share would generate between $1.6 billion and $2.2 billion a year. The midpoint of this estimate was $1.9 billion. This estimate used 2015 income data that DOR adjusted to better reflect what the anticipated income from Fair Share would be in 2019. (This estimate was produced in response to a previous proposal for a millionaire tax in Massachusetts.) Adjusting this estimate using the rate of growth of personal income tax revenue from 2019 (actual) through 2023 (estimated), MassBudget calculates that DOR's 2019 $1.9 billion annual estimate would increase to more than $2.5 billion in 2023.

As with all its revenue estimates, DOR provided a "static" analysis of Fair Share. DOR did not undertake a "dynamic" analysis, meaning they did not attempt to account for potential changes in taxpayer behavior that could result from the proposed tax change. Such responses could include an increase in tax avoidance, tax filers moving to other states, as well as the revenue implications of affected filers' cutting back on their spending or investment. Similarly, DOR did not include in its analysis any potential revenue gains from the well-documented positive economic impacts of increased government investment in education and transportation.

The Center for State Policy Analysis (cSPA) at Tufts University released a report in January 2022 that presented both a static and a limited dynamic revenue gain estimate of Fair Share. cSPA's static estimate concludes that Fair Share would generate $2.1 billion annually, beginning in 2023. cSPA's dynamic analysis, however, finds that Fair Share would result in a combination of a) a very modest number of Massachusetts high-income households moving out of state and, far more importantly, b) a large increase in affected tax filers' efforts to avoid paying the tax. cSPA estimates that together, these behavioral responses would reduce the amount of new revenue generated by Fair Share by more than a third, to $1.3 billion. Although the cSPA report notes the beneficial economic effects of increased state spending on education and transportation, cSPA's dynamic analysis does not appear to include potential revenue gains driven by this additional state spending.

The Institute on Taxation and Economic Policy (ITEP) is a D.C. think tank with widely recognized expertise in modeling the revenue and distributional impacts of state and federal tax policies. Using projected 2023 incomes, ITEP estimates that Fair Share would generate $2.7 billion per year in new revenue. This is a static estimate.

A CLOSER LOOK AT "DYNAMIC FACTORS" THAT MIGHT AFFECT TAX COLLECTIONS

Adjusted for projected 2023 income levels, all three analyses produce static revenue gain estimates above $2 billion, ranging from $2.1 billion to $2.7 billion per year.

Unique among the three, cSPA provides an additional, dynamic analysis, looking at possible changes in taxpayer behavior that would reduce expected revenue gains. cSPA notes that the increase in out-migration (or "tax flight") is likely to be small. Settling on a rough midpoint among several academic studies with widely varying results, cSPA concludes that Fair Share would lead to a significant rise in tax avoidance. cSPA estimates that greater tax avoidance alone would reduce the amount of additional revenue Fair Share would generate by some 30 percent. (Even still, cSPA estimates that Fair Share would generate an additional $1.3 billion annually.) A surge in tax avoidance of this magnitude, however, seems unlikely. Indeed, one study cSPA considers suggests a reduction in revenue only a quarter as large.

For many high-income Massachusetts filers, the 4-percentage point rate increase that Fair Share would impose (only on the portion of income above $1 million) represents a relatively small increase in their current combined top state and federal income tax rate of 42 percent (5 percent state rate + 37 percent federal top rate). This relatively small increase provides little added incentive for taxpayers to seek additional – and likely riskier – tax avoidance strategies.

It also is unlikely that high-income filers have many additional options for significantly increasing their tax avoidance. Most high-income filers already hire tax accountants and/or tax lawyers to reduce their state and federal tax liabilities to the legal minimum. Presumably, these tax specialists already have identified and maximized their clients' existing legal opportunities to avoid paying taxes.

It is unclear either why Fair Share would generate a substantial, new appetite for tax avoidance (see above) or how accountants and lawyers could satisfy any such appetite without crossing the line from tax avoidance into tax evasion. While tax avoidance is legal, tax evasion carries the possibility of criminal penalties for taxpayers and their tax preparers alike. Notably, the recently passed federal Inflation Reduction Act of 2022 provides substantial new funding for the IRS. In particular, there is new funding to increase the number and quality of audits the IRS conducts on corporations and high-income filers. This is expected to reduce current levels of tax avoidance among these filers, resulting in significant revenue gains at the federal level.

Further, to the extent that a modest portion of expected revenue gains from Fair Share are lost due to out-migration and tax avoidance, it also is the case that increased state investment in the education and transportation sectors will generate some additional, offsetting revenue gains.

Considering the above, MassBudget concludes that a figure of $2 billion represents a reasonable – and even a conservative – estimate of the additional net revenue Fair Share would generate annually for investments in education and transportation.