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November 10, 2015

State Tax Panel
C/o Mary E. Finnegan, State Tax Panel Administrator
State Capitol Building, Room 501
Hartford, CT 06106

Dear Senator Bill Nickerson, Representative Bill Dyson, and Distinguished Members of the Panel:

The impact of Connecticut's tax system on migration has been at the forefront of discussions among presenters and members of the State Tax Panel.

In furtherance of this discussion, we offer the attached report from Yale Law School's Legislative Advocacy Clinic, as reviewed and edited by Connecticut Voices for Children. This report compares multi-state tax policies (estate, income, inheritance); assesses the relationship between tax changes and population migration; and recommends a specific course of action for the state that is consistent with the overarching principles of transparency, equity and sustainability articulated by the panel.

The report looks at the year-on-year taxpayer migration data mentioned before the panel and finds that, within the limits of the use of such data in assessing change over time, Connecticut and other New England states with more robust estate taxes have actually outperformed their lower-estate-tax neighbors in year-to-year growth in adjusted gross income.

In Connecticut, while 300 fewer returns were filed in 2013 than in 2012, the total tax revenue generated increased by nearly $10 billion, from $139.6 billion to $149.3 billion (an increase of 6.28%). This rate of increase puts Connecticut ahead of its lower-tax regional peers such as New Hampshire, which experienced markedly slower growth in taxable income.

Overall Adjusted Gross Income (AGI) of All State Taxpayers
Percentage Change of Connecticut and Peer States between 2012 and 2013

	Percentage Change	**Estate Tax Regime Type (at time data was gathered on 1/1/2013)**
Massachusetts	7.49%	$1M min. size, rates .8%-16%
Connecticut	6.28%	$2M min. size, rates 7.2% - 12%
Maine	5.74%	$1M min. size, rates 8.0%-12%
New Hampshire	5.56%	**NONE**
Vermont	5.4%	$2.75M min. size, rates .8%-16%
Rhode Island	4.55%	$921,000 min. size, rates .8%-16%

Source: Internal Revenue Service - SOI Tax Stats - Migration Data

When limiting the data to individuals earning over $200,000 per year (those most likely to consider the impact of an estate tax), the number of returns increased by 6,880 and the total AGI increased by $9.2 billion.

Overall Adjusted Gross Income (AGI) of Taxpayers with Income above $200,000
Percentage Change of Connecticut and Peer States between 2012 and 2013

	Percentage Change	**Estate Tax Regime Type (at time data was gathered on 1/1/2013)**
Maine	23.26%	$1M min. size, rates 8.0%-12% (at $10M)
Vermont	18.01%	$2.75M min. size, rates .8%-16%
Massachusetts	16.85%	$1M min. size, rates .8%-16% (at $10M)
Connecticut	15.98%	$2M min. size, rates 7.2% - 12% (at $10M)
New Hampshire	15.6%	**NONE**
Rhode Island	14.94%	$921,000 min. size, rates .8%-16% (at $10M)

Source: Internal Revenue Service - SOI Tax Stats - Migration Data

The data do not support a conclusion that high-income individuals are fleeing the state. To the contrary, the data suggest that, among Connecticut's peer states, those which fared best in terms of total AGI growth were those with more progressive estate taxes.

Thank you for your time. We would be happy to answer any questions.

Sincerely,

Ellen Shemitz, Executive Director
Connecticut Voices for Children
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Daniel Rauch
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Daniel E. Rauch November 10, 2015

Memorandum: Analysis and Proposals for Progressive Estate, Gift, and/or Inheritance Taxes

Prepared in conjunction with the Yale Law School Legislative Advocacy Clinic

This document serves four main purposes: first, it provides background material on state-level estate taxes and inheritance taxes [hereinafter EI taxes]. Second, it highlights key sources in the available secondary literature of EI taxes. On balance, these sources conclude that there is no compelling evidence that progressive EI tax regimes cause outmigration, yet there is considerable evidence that EI taxes can offer states valuable revenue sources. Third, using the most recent available IRS migration data, this document analyzes the current impact of Connecticut's EI taxes in contributing to possible outmigration, with a special focus on how such taxes impact various demographic and economic subgroups. Finally, the document offers a set of proposals by which Connecticut's current EI regime might be altered to help raise state revenue while adhering to the core values of transparency, equity and sustainability.

I. Overview of State EI Taxation

This section offers background information on how states currently implement state-level EI taxation. It also offers a somewhat more detailed overview of Connecticut's current EI tax regime.

A. Brief Overview and Background on State Estate Taxes

Federal-level estate taxes have been imposed intermittently since early in American history,[1] and became formalized early in the twentieth century.[2] At the end of the twentieth century, state estate taxes in all 50 states took the same form due to a particular feature of the Federal estate tax:

> For most of its history, the Federal estate tax system has included a provision that allowed a Federal estate tax credit for any state estate taxes that were paid. A mechanism for avoiding double taxation, the credit ensured that any Federal estate tax obligations would only be for the excess above the liability at the state level.
>
> For instance, if the state estate tax was $100,000 and the Federal estate tax was $400,000, then a $100,000 credit would be applied at the Federal level, reducing the obligation to only $300,000. The net result - the *total* taxes owed remain at $400,000 (the Federal estate tax amount), but the *actual* taxes paid will be $100,000 to the state and the *remaining* $300,000 to the Federal

[1] Robert Yablon, *Defying Expectations: Assessing The Surprising Resilience Of State Death Taxes, Tax Lawye*r 59 Tax Lawyer 241, 244 (2005).
[2] *Id.*

> government.
>
> Of course, this would theoretically provide an incentive for states to just increase their state estate tax all the way up to the Federal level – thereby capturing all of the Federal estate tax without actually increasing what citizens would owe in total - so the Federal system under IRC Section 2011 put a cap in place, with a maximum tax rate of 16% on estates just over $10M of net worth.
>
> Nonetheless, states took advantage of the available credit to the extent they could; for many decades, every state had a "sponge" estate tax that, by statute, applied a state level tax that was exactly equal to the maximum amount allowed as a credit under the Federal system. This essentially made the Federal estate tax system a Federal-state "partnership" of sorts, as states had free reign to gather a portion of the Federal estate tax without actually increasing anyone's total tax obligations, as all of the state estate tax was effectively "carved out" of the Federal obligation due to the available credit.[3]

Accordingly, the state statutes that provided for EI taxes were "sponge taxes,"[4] textually linked to the federal tax credit. For example, consider Idaho's estate tax statute:

> (1) A tax in an amount equal to the federal credit is imposed on the transfer of the taxable estate of every resident.[5]

In 2001, however, the federal government adopted the Economic Growth and Tax Relief Reconciliation Act of 2001 [EGTRRA].[6] This legislation abolished the original state-level EI credit. In its place, it offered a deduction for individual taxpayers. As a result, the previous regime of state EI taxes, which had been premised on the existence of the federal credit program, effectively became a dead letter.

In response to this 2001 change, each state adopted one of four approaches: (1) first, some states used this shift as occasion to affirmatively abolish their own estate tax laws. (2) Second, some states did nothing, leaving their original, federally-linked laws in place. To date, the functional outcome in such states has been the same as abolition: no federal credit is on offer, so no state estate tax is being collected. However, were the federal government to re-enact such credits, presumably these "dormant" EI taxes would come back into effect. That said, the legislative prospects of such a change seem somewhat remote.[7] (3) Third, some states, often referred to as "pick up" states, adopt schemes "that continue to impose

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[3] Michael Kitces, "The Untenable State Of State Estate Taxes – Recouple, Repeal, Or Enact Gift Taxes," Nerd's Eye View, https://www.kitces.com/blog/the-untenable-state-of-state-estate-taxes-recouple-repeal-or-enact-gift-taxes/.

[4] So-named because they "soaked up" all available federal estate tax credit.

[5] Idaho Code Ann. § 14-403 (West).

[6] Pub. L. No. 107-16, 115 Stat. 38.

[7] *See, e.g.*, Steven Roll, State Tax Snapshot: State Death Tax Credit Is Tossed Over The Fiscal Cliff, BloombergBNA (Jan 7, 2013), http://www.bna.com/state-tax-snapshot-b17179871728/.

an estate tax . . . based on the graduated schedule of the pre-EGTRRA version of the I.R.C. § 2011 credit for state death taxes, with levels of exemption ranging from $675,000 to $3,500,000."[8] (4) Finally, some states, like Connecticut, "decoupled" their EI systems from federal law by adopting a standalone tax.[9]

In any case, as of January 1, 2015, 16 states and the District of Columbia have state-level[10] estate taxes, while 6 states have inheritance taxes.[11] A full overview of these states (not including states that have only a "dormant" federally-linked EI tax statute) is presented in Appendix A at the conclusion of this document.

[8] Susan K. Dromsky-Reed et al., "State Death Taxes in Uncertain Times," American Bar Association, available at http://www.americanbar.org/content/dam/aba/publishing/rpte_ereport/te_dromsky_harding_and_rosenberger.authcheckdam.pdf.

[9] To be sure, if the federal government altered the current federal estate tax structure in a significant way, this would have potentially substantial consequences for the ways in which states collect EI taxes. Currently, no such changes seem likely. *See* Steven Roll, State Tax Snapshot: State Death Tax Credit Is Tossed Over The Fiscal Cliff, BloombergBNA (Jan 7, 2013), http://www.bna.com/state-tax-snapshot-b17179871728/. However, though such possibilities are remote, they should still be carefully monitored. *See* the policy recommendations of this document.

[10] Or, in the case of Washington, D.C., "district level."

[11] Tax Foundation, Facts and Figures 2015: How Your State Compare, http://taxfoundation.org/sites/taxfoundation.org/files/docs/Fact%26Figures_15_web_9_2.pdf tbl 34-35.

B. Connecticut's Current EI Tax Regime

Currently, Connecticut levies an estate tax, with an exemption for all states below $2 million dollars. The current tax structure imposes rates ranging from 7.2% to 12%. The rates are organized as follows:[12]

Amount of Taxable Estate	Amount Due on Death of Decedent
Not over $2,000,000	None
Over $2,000,000 but not over $3,600,000	7.2% of the excess over $2,000,000
Over $3,600,000 but not over $4,100,000	$115,200 plus 7.8% of the excess over $3,600,000
Over $4,100,000 but not over $5,100,000	$154,200 plus 8.4% of the excess over $4,100,000
Over $5,100,000 but not over $6,100,000	$238,200 plus 9.0% of the excess over $5,100,000
Over $6,100,000 but not over $7,100,000	$328,200 plus 9.6% of the excess over $6,100,000
Over $7,100,000 but not over $8,100,000	$424,200 plus 10.2% of the excess over $7,100,000
Over $8,100,000 but not over $9,100,000	$526,200 plus 10.8% of the excess over $8,100,000
Over $9,100,000 but not over $10,100,000	$634,200 plus 11.4% of the excess over $9,100,000
Over $10,100,000	$748,200 plus 12% of the excess over $10,100,000

The current structure is the result of several pieces of legislation. As noted above, Connecticut – along with 49 other states – originally had a "sponge" estate tax, designed explicitly to "soak up" the available federal credit. With the passage of EGTRRA, which wiped out the federal credit, the state was left to devise a standalone tax. It did so in 2005.[13] Since then, there have been several legislative changes to this standalone tax regime. The minimum taxable estate size has shifted from $2 million to $3.5 million and,[14] most recently, back to $2 million. This shift is important, if only because it demonstrates that minimum exemptions need not be "one-way ratchets," but rather, can be brought down as well as up.

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[12] Data from Connecticut Estate and Gift Tax Return and Instructions, Connecticut Department of Revenue, http://www.ct.gov/drs/lib/drs/forms/2014forms/estateandgifttax/2014-ct-706-709-booklet.pdf

[13] PA 05-251.

[14] PA 11-6, as amended by PA 11-61.

More recently, legislation has capped the total amount of tax that any estate can be required to pay at $20 million.[15] Additionally, the marginal rate has changed somewhat over time.

It is also noteworthy that Connecticut's EI structure uses a unified gift/estate tax. Under this "unified" transfer tax system:

> [L]ifetime gifts count against a threshold of $2 million, but the $2 million also includes the amount that passes through your estate after your death. That is, if your total lifetime gifting added to the value of your estate exceeds $2 million, a transfer tax (estate and gift) will be due to the state of Connecticut. However, [gifts falling below the federal gift tax's annual exclusions] of $14,000 are exempt from Connecticut gift taxes.[16]

In any event, in 2013-2014, EI taxes contributed some $168 million to Connecticut's general fund revenue – contributing roughly 1.12% of Connecticut's after-refund tax revenue.[17]

Moreover, the Connecticut's Department of Revenue Services tax incidence study indicates that the incidence of the estate tax, as compared to other taxes, like income taxes, is highly progressive.[18] In particular, gift and estate taxes fell on just .9% of CT households.[19] Moreover, the report noted that "[t]he Suits Index of 0.76 for this tax indicates that the tax is very progressive. The impact of this tax is entirely borne by the households in the top three income deciles." Indeed, "The Personal Income Tax . . . and the Gift and Estate Tax . . . are the only two [Connecticut] taxes classified as progressive."[20]

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[15]PA 15-244, §§ 174 & 175.

[16] Julie Jason, "All About the gift tax," CTPost (July 4, 2015), http://www.ctpost.com/business/article/Julie-Jason-All-about-the-gift-tax-6364019.php. The need for such "unified" gift/estate taxes is heavily influenced by a key federal-level change. The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act (also known as the first "fiscal cliff" legislation), increased the federal *gift* tax exemption from $1 million to $5 million. This is significant, because in states that have an inheritance or estate tax but no gift tax, a substantial loophole had opened: individuals could simply give away their money before death and, so long as the amount given was below 5 million, they would be immune from state estate or inheritance taxation. States have responded to this new loophole in a number of ways, such as by the use of "gift-in-contemplation-of-death" rules that count gifts given shortly before death as part of the estate for tax purposes or by the enactment of new state gift taxes (as occurred recently in Minnesota). However, many other states have yet to fully grapple with the ramifications of this change. Note, though, that insofar as Connecticut already has a state-level gift tax, this loophole is not relevant to the current set of recommendations.

[17] Connecticut FY 2016 – FY 2017 Biennium Governor's Budget Summary, http://www.ct.gov/opm/lib/opm/budget/2016_2017_biennial_budget/budget/section_a.pdf, at A-8.

[18]Connecticut Department of Revenue Services, Connecticut Tax Incidence, Dec. 2014, at 7, 15, available at http://www.ct.gov/drs/lib/drs/DRSTaxIncidenceReport2014.pdf.

[19] *Id.* at 7.

[20] *Id.* at 15.

II. Secondary Literature on EI Taxation

This section gathers the key overall secondary literature on EI taxation. Notwithstanding colorful anecdotes to the contrary,[21] on the whole state-level EI taxation appears to be effective in raising revenue, and does not have the dramatic out-migration effects that critics claim it does.[22] For particularly cogent and comprehensive treatments of this empirical problem, see sources including:

Robert Tannenwald et al.*, Tax Flight Is A Myth*, Center on Budget and Policy Priorities, Aug. 5, 2011, http://www.cbpp.org/research/tax-flight-is-a-myth.

Marius Brülhart & Raphaël Parchet, *Alleged tax competition: The mysterious death of bequest taxes in Switzerland*. Journal of Public Economics 111 (2014)

Karen Smith Conway & Jonathan Rork "State 'Death' Taxes and Elderly Migration – The Chicken or the Egg?," 59 National Tax Journal 97 (2006).

Karen Smith Conway & Jonathan Rork, "No Country for Old Men (Or Women) – Do State Tax Policies Drive Away the Elderly?" University of New Hampshire Working Paper, April 2010.

Michael Mazerov, State Taxes Have a Negligible Impact on Americans' Interstate Moves, May 21, 2014, Center on Budget and Policy Priorities, http://www.cbpp.org/research/state-budget-and-tax/state-taxes-have-a-negligible-impact-on-americans-interstate-moves,

Jeffrey Thompson, The Impact Of Taxes On Migration In New England, Working Paper, Political Economy Research Institute University of Massachusetts, Amherst April 2011. http://www.peri.umass.edu/fileadmin/pdf/published_study/Migration_PERI_April13.pdf.

Cristobal Young et al., Millionaire Migration and the Taxation of the Elite: Evidence from Administrative Data, Dec. 8, 2014,

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[21] *See, e.g.*, wills.about.com/b/2013/05/13/moving-to-avoid-estate-taxes-and-income-taxes-absolutely-says-one-maryland-couple.htm.

[22] This memo does not consider the question of the optimal level or extent of the federal estate tax. For contributions to that debate, *see* Mariacristina De Nardi & Fang Yang, Wealth Inequality, Family Background, And Estate Taxation, NBER Working Paper Series, http://www.nber.org/papers/w21047; *see also* Chye-Ching Huang & Brandon Debot, Ten Facts You Should Know About the Federal Estate Tax, Center on Budget and Policy Priorities, Mar. 23, 2015, http://www.cbpp.org/research/ten-facts-you-should-know-about-the-federal-estate-tax.

http://web.stanford.edu/~cy10/public/Millionaire_Migration_and_the_Taxtion_of_the_Elite.pdf.

Cristobal Young & Charles Varner, *Millionaire Migration And State Taxation Of Top Incomes: Evidence From A Natural Experiment*, National Tax Journal, June 2011, 64 (2, Part 1), 255–284, available at http://web.stanford.edu/~cy10/public/Millionaire_Migration.pdf.

While these sources each vary slightly in their emphasis, they suggest a broad consensus that estate tax increases do not meaningfully contribute to increased outmigration to other states, but do raise valuable revenue.

* * * * *

Against this consensus, several state-level studies purport to show serious negative effects from EI taxation. These studies have all followed a remarkably similar pattern: in each case, a conservative group has undertaken the research, often with prominent ties to political officials, and often without much in the way of serious analytical credentials. And in each case, the underlying research has been found to contain serious methodological errors. Several of the more prominent examples of such state-specific studies are worth investigating more closely: "The Economic Consequences of Tennessee's Gift and Estate Tax" [hereinafter "Tennessee Study"],[23] "Exodus on the Parkway: Are Taxes Driving Wealthy Residents out of New Jersey?" ["New Jersey study"],[24] and a recent report by the Yankee Institute about Connecticut ["Yankee Institute Report"].[25]

On the whole, however, each of these studies suffers serious methodological flaws which makes their conclusions untenable.[26]

A. The Tennessee Study

One paradigmatic study critiquing state estate taxes was produced during the (ultimately successful) campaign to repeal Tennessee's EI tax regime: "The Economic Consequences of

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[23] A.B. Laffer et al., The Economic Consequences of Tennessee's Gift and Estate Tax, Beacon Center of Tennessee, March 2012, http://www.beacontn.org/wp-content/uploads/The-Economic-Consequences-of-Tennessees-Gift-Estate-Tax.pdf.

[24] Eric Furey et al., *Exodus on the Parkway: Are Taxes Driving Wealthy Residents out of New Jersey? The Impact that Incentives and Taxes Have on Choice of Domicile*, Regent Atlantic, Jan. 2014, https://www.regentatlantic.com/File%20Library/Tax%20paper/Exodus-on-the-Parkway-2-25-14-FINAL-VERSION.pdf.

[25] Suzanne Bates, *High Taxes Hurt*, Yankee Institute Policy Report Feb. 11, 2015, available at http://www.yankeeinstitute.org/policy-briefs/high-taxes-hurt-2/.

[26] Other examples in the genre, which have not yet received a sustained counter-attack but which rely on the same sorts of methodological problems that plague better-publicized state studies, include Peter J. Nelson, Do Minnesotans Move to Escape the Estate Tax? The weight of the evidence points to a strong yes, Center of the American Experiment (March 5, 2015).

Tennessee's Gift and Estate Tax."[27]

In brief, the Tennessee Study asserts that if "Tennessee's estate tax had been repealed 10 years ago, the state's economy would have been unleashed, and would have grown . . . at a rate exactly equal to the average among states not levying an income tax."[28]

The Tennessee Report specifically relied on two data points: "(1) In 2009, Florida had almost twice as many federal estate tax returns filed, on a per capita basis, than Tennessee," and "(2) In 2009, the average value of an estate in Florida was roughly 67 percent higher than in Tennessee."[29]

Yet this analysis is deeply misleading, for as critics have noted, "Florida had almost twice as many federal estates filed per 100,000 population than Tennessee . . . But this is not particularly surprising given the state's well-known appeal to retirees with the financial means to follow the sun. And . . . this discrepancy was actually *larger* before Florida's estate tax began to disappear in 2002 as a result of the federal Bush tax cuts."[30] Moreover, there is no sustained evidence that the value of Tennessee estates relative to Florida estates was in any way impacted by the estate tax.[31]

B. The New Jersey Study

New Jersey's EI regime is arguably the nation's most progressive. In particular, the minimum size of taxable estates in the Garden State is only $675,000, considerably lower than Connecticut's minimum of $2 million.

Unsurprisingly, conservative groups and publications have repeatedly identified it as the "worst" or "scariest" EI regime in the country,[32] while Garden State Republicans have repeatedly tried to curtail or repeal the tax. This effort culminated in a report similar to the Tennessee Study: "Exodus on the Parkway: Are Taxes Driving Wealthy Residents out of New Jersey?" [the "New Jersey study"].[33]

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[27] A.B. Laffer et al., The Economic Consequences of Tennessee's Gift and Estate Tax, Beacon Center of Tennessee, March 2012, http://www.beacontn.org/wp-content/uploads/The-Economic-Consequences-of-Tennessees-Gift-Estate-Tax.pdf..

[28] Institute on Taxation and Economic Policy, "Repealing Estate Tax Will Not Create An Economic Boom," April 2012, http://www.itep.org/pdf/lafferestate0412.pdf.

[29] *Id.*

[30] *Id.* at 3 (emphasis in original).

[31] *Id.*

[32] *E.g.*, "10 States With the Scariest Death Taxes," Kiplinger, http://www.kiplinger.com/slideshow/taxes/T021-S003-states-scariest-death-taxes-estate-inheritance/index.html.

[33] Eric Furey et al., *Exodus on the Parkway: Are Taxes Driving Wealthy Residents out of New Jersey? The Impact that Incentives and Taxes Have on Choice of Domicile*, Regent Atlantic, Jan. 2014, https://www.regentatlantic.com/File%20Library/Tax%20paper/Exodus-on-the-Parkway-2-25-14-FINAL-VERSION.pdf.

The most comprehensive available analysis, however, suggests that New Jersey's EI taxes do not have this effect and, instead, yield substantial revenue for the state.[34]

C. The Yankee Institute Report

Closer to home, in 2015 the conservative Yankee Institute published a study purporting to show the "disaster[ous]" consequences of Connecticut's EI regime.[35] As one commentator summarized:

> In a paper published early in 2015, the Yankee Institute for public policy asserted that people moving out of Connecticut "represent lost tax revenue." And in a statement to the State Tax Panel on September 16, 2015, the Institute's Policy Director observed that according to data from the Internal Revenue Service, about 15,000 more individuals left the state than moved into the state – and the difference in AGI [annual gross income] reported for 2013 for the filers who left the state totaled about $1.9 billion more than the AGI reported for 2013 for the filers who moved into the state. Based on this report, the Policy Director indicated that a "disaster" was in the offing.[36]

Such allegations have been perennially made by Connecticut's EI tax opponents.[37] However, the Yankee Institute report ultimately wilts under close scrutiny. As Bill Cibes explains, a closer look at the IRS data on which the report was based shows that:

> [T]he actual data reported by the IRS show that, even after these out-migrants left the state, the total AGI for all Connecticut residents in 2013 was about $9.7 billion **more** than the AGI for Connecticut residents in 2012. Although, in total, there were about 300 fewer returns filed in Connecticut in 2013 than in 2012 (with about 10,000 fewer exemptions claimed), the total AGI reported on those returns was about $149.3 billion in 2013, as opposed to $139.6 billion in 2012.
>
> And for those with considerable income (>$200K), about 6,000 more returns in this income class were filed in 2013 than in 2012, and the total AGI reported for this category was about $9.2 billion **more** in 2013 than in 2012. That is, although out-migration exceeded in-migration from 2012 to 2013, there appears to have been no income lost as a result of that out-migration.

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[34] Jon Whiten, Levied on Very Few, New Jersey's Estate and Inheritance Taxes Support Colleges, Health Care & Other Services, New Jersey Policy Perspective, http://www.njpp.org/reports/levied-on-very-few-new-jerseys-estate-and-inheritance-taxes-support-colleges-health-care-other-services.

[35] Suzanne Bates, *High Taxes Hurt*, Yankee Institute Policy Report Feb. 11, 2015, available at http://www.yankeeinstitute.org/policy-briefs/high-taxes-hurt-2/.

[36] Bill Cibes, Voices For Children, e-mail analysis on file with author.

[37] *See, e.g.*, Testimony of Mark Pruner, Connecticut Licensed Real Estate Agent in support of SB 367, Connecticut Finance Revenue and Bonding Committee Public Hearing, Mar. 13, 2012.

> Or if some income did walk out the door, it was more than replaced by the growth in income of those who stayed in the state, or moved in.
>
> Without exception, the total AGI for all taxpayers with income greater than $200,000, for all of the various age ranges, was higher – after out-migration – than it was in 2012.
>
> Without exception, the number of returns, and the number of exemptions reported on those returns, for taxpayers with income greater than $200,000 increased from 2012 to 2013, for all of the various age ranges.
> Except for age ranges 36-45 and 46-55, the total AGI for taxpayers with income from $100,000 to $200,000 was higher in 2013 than in 2012, and the number of taxpayers and the number of exemptions increased.
>
> The greatest decreases from 2012 to 2013 in number of filers, and the number of exemptions, were in age ranges 36-45 and 46-55 (except for taxpayers with income greater than $200,000, where there was no erosion). There was a very slight decrease in total AGI for filers in age range 36-45, but a small increase in total AGI for filers in age range 46-55.
>
> For age ranges 56-65 and over 65, the total number of returns, the total number of exemptions and the total AGI for these age ranges all increased from 2012 to 2013 – although, in general, this was not the case for taxpayers in the three income classes with less than $50,000 income. [38]

Accordingly, the Connecticut study, like its predecessors from other states, is ultimately misleading.

III. Quantitative Analysis of Connecticut's EI Taxation

This section builds on the existing secondary literature by offering a novel analysis of Connecticut's demographic and tax data to explore the impact of state EI taxes. This analysis ultimately suggests that the impact of EI taxes on outmigration and on revenue losses poses no significant problem.

The most comprehensive source of relevant information stems from the IRS's migration data. Unfortunately, the only years currently available are for 2012 and 2013. Nonetheless, this is the data that the Yankee Institute and other opponents of the Estate Tax have relied on, and may shed light onto the impact of Connecticut's estate tax regime.

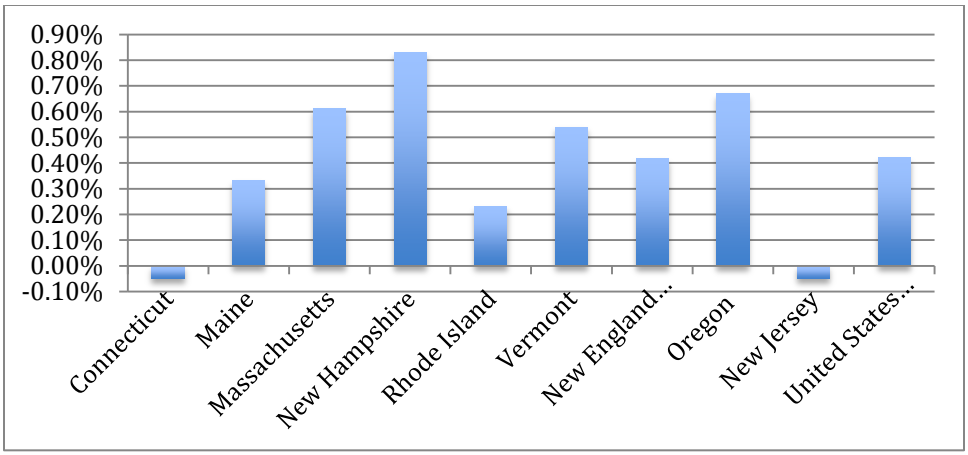
The states analyzed included all of the states in the New England region (Connecticut, Maine, Massachusetts, New Hampshire, Rhode Island, and Vermont). A regional New England average is included as well. Notably, of these states, New Hampshire has no EI taxes, making it a useful comparison point. Also included are two other states with

[38] Cibe, on file with author

substantially progressive EI tax regimes: Oregon and New Jersey. Finally, a national average is added for reference.

Note that some states EI tax regime has changed in the time since the 2012-2013 data was gathered. Wherever possible, this chart uses the tax regime in effect at that time.

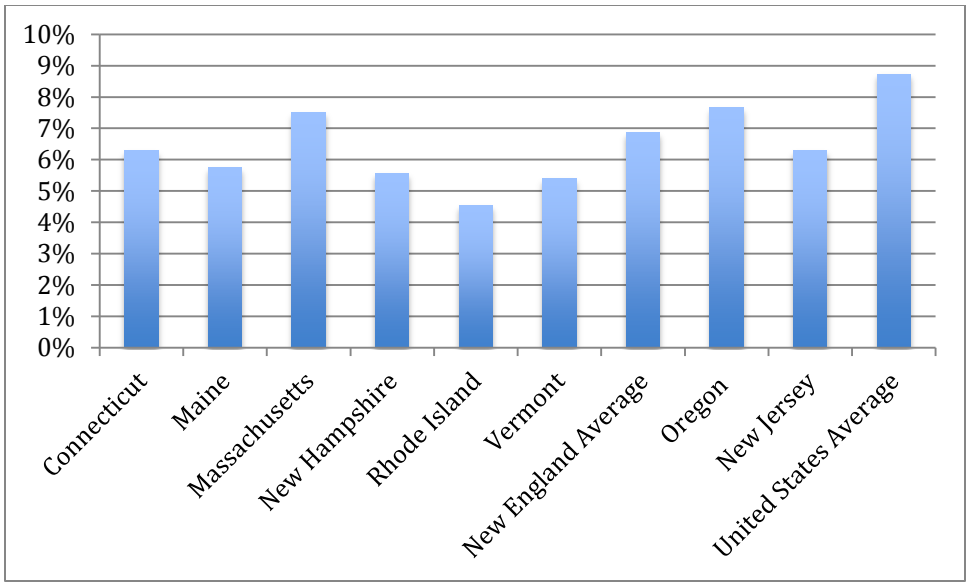
(1) Overall Number of Tax Returns Filed, Percentage Change Between 2012 and 2013



	Percentage Change	Estate Tax Regime Type at time IRS data gathered (1/1/2013)
Connecticut	-0.05	$2M min. size, rates 7.2% - 12% (at $10M)
Maine	0.33	$1M min. size, rates 8.0%-12% (at $10M)
Massachusetts	0.61	$1M min. size, rates .8%-16% (at $10M)
New Hampshire	0.83	**NONE**
Rhode Island	0.23	$921,000 min. size, rates .8%-16% (at $10M)
Vermont	0.539	$2.75M min. size, rates .8%-16%
New England Average	0.417	N/A
Oregon	0.67	$1M min. size, rates 10%-16% (at $9.5M)
New Jersey	-0.05	$675,000 min. size, rates 4.8%-16% (on $10M)
United States Average	0.42	N/A

It is clearly correct that Connecticut's amount of returns dropped, and that Connecticut's Estate tax is relatively progressive.

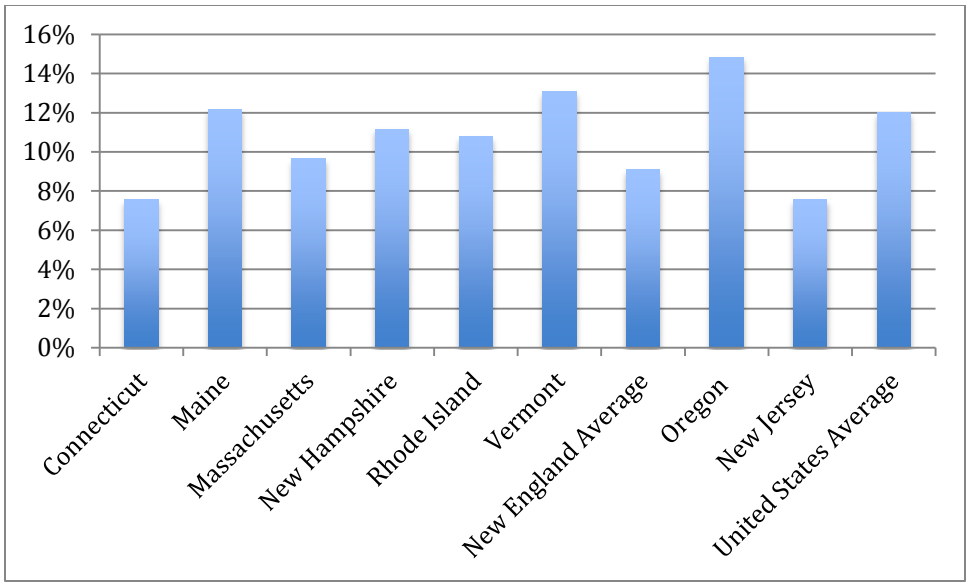
(2) Overall Adjusted Gross Income (AGI) of all taxpayers, Percentage Change Between 2012 and 2013



	Percentage change	Estate Tax Regime Type at time IRS data gathered (1/1/2013)
Connecticut	6.28	$2M min. size, rates 7.2% - 12% (at $10M)
Maine	5.74	$1M min. size, rates 8.0%-12% (at $10M)
Massachusetts	7.49	$1M min. size, rates .8%-16% (at $10M)
New Hampshire	5.56	**NONE**
Rhode Island	4.55	$921,000 min. size, rates .8%-16% (at $10M)
Vermont	5.4	$2.75M min. size, rates .8%-16%
New England Average	6.87	N/A
Oregon	7.65	$1M min. size, rates 10%-16% (at $9.5M)
New Jersey	6.28	$675,000 min. size, rates 4.8%-16% (on $10M)
United States Average	8.733	N/A

However, even as the amount of taxpayers has slightly declined, the overall amount of income generated has increased. Strikingly, it has increased at a faster rate than that of New Hampshire, a peer state with no estate tax.

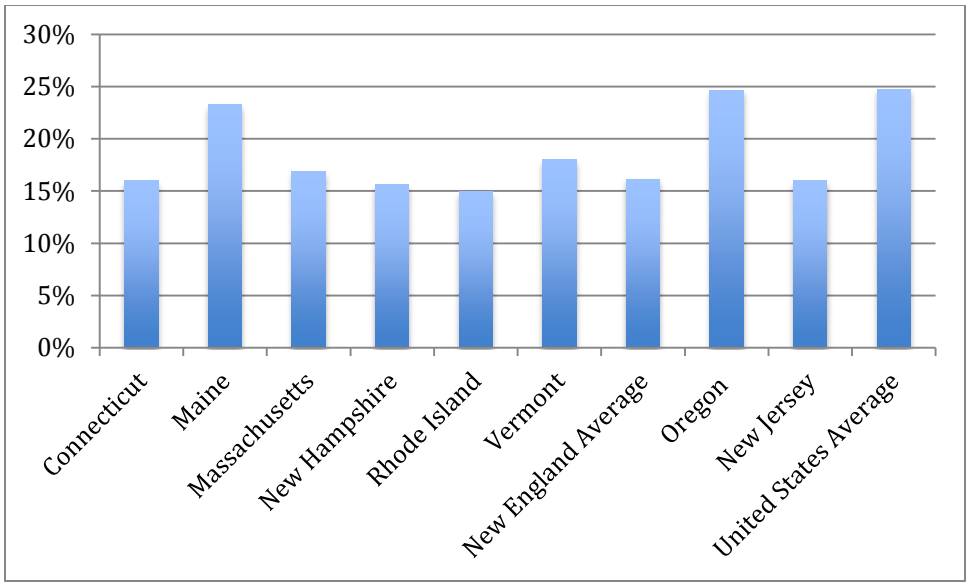
(3) Overall Number of Returns Filed by Taxpayers with Income Above $200,000 Percentage Change Between 2012 and 2013



	Percentage change	Estate Tax Regime Type at time IRS data gathered (1/1/2013)
Connecticut	7.56	$2M min. size, rates 7.2% - 12% (at $10M)
Maine	12.18	$1M min. size, rates 8.0%-12% (at $10M)
Massachusetts	9.64	$1M min. size, rates .8%-16% (at $10M)
New Hampshire	11.16	**NONE**
Rhode Island	10.8	$921,000 min. size, rates .8%-16% (at $10M)
Vermont	13.06	$2.75M min. size, rates .8%-16%
New England Average	9.102	N/A
Oregon	14.83	$1M min. size, rates 10%-16% (at $9.5M)
New Jersey	7.57	$675,000 min. size, rates 4.8%-16% (on $10M)
United States Average	12	N/A

Meanwhile, Connecticut has seen an increase in the number of taxpayers making more than $200,000 a year.

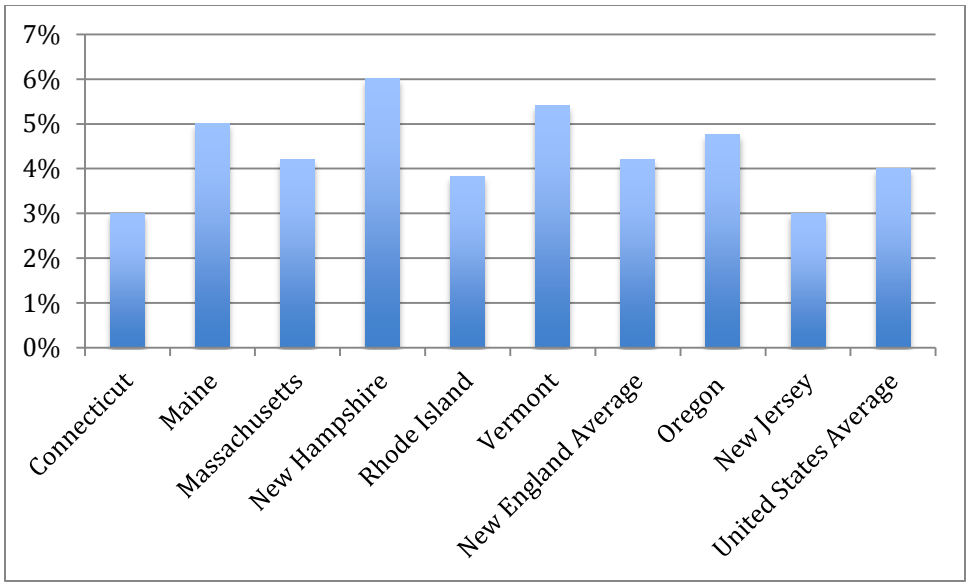
(4) Overall Adjusted Gross Income (AGI) of all taxpayers with Income Above $200,000 Percentage Change Between 2012 and 2013



	Percentage Change	Estate Tax Regime Type at time IRS data gathered (1/1/2013)
Connecticut	15.98	$2M min. size, rates 7.2% - 12% (at $10M)
Maine	23.26	$1M min. size, rates 8.0%-12% (at $10M)
Massachusetts	16.85	$1M min. size, rates .8%-16% (at $10M)
New Hampshire	15.6	**NONE**
Rhode Island	14.94	$921,000 min. size, rates .8%-16% (at $10M)
Vermont	18.01	$2.75M min. size, rates .8%-16%
New England Average	16.14	N/A
Oregon	24.66	$1M min. size, rates 10%-16% (at $9.5M)
New Jersey	15.98	$675,000 min. size, rates 4.8%-16% (on $10M)
United States Average	24.75	N/A

And, the increase in income of those making more than 200,000 is line with the rest of the region, and exceeds comparable levels in low-estate-tax New Hampshire.

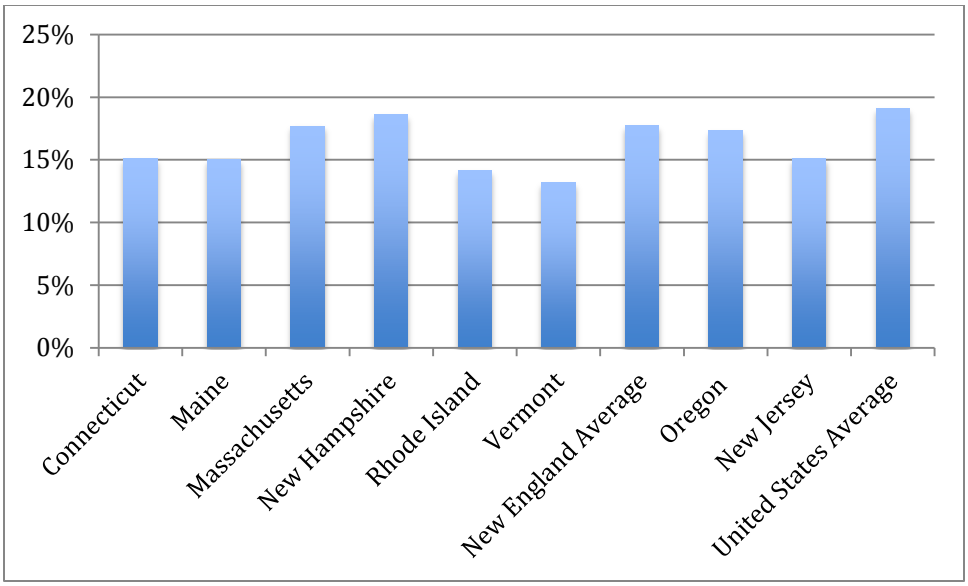
(5) Overall Number of Returns Filed by Taxpayers Over 65, Percentage Change Between 2012 and 2013



	Percentage Change	Estate Tax Regime Type at time IRS data gathered (1/1/2013)
Connecticut	3	$2M min. size, rates 7.2% - 12% (at $10M)
Maine	5	$1M min. size, rates 8.0%-12% (at $10M)
Massachusetts	4.2	$1M min. size, rates .8%-16% (at $10M)
New Hampshire	6.02	**NONE**
Rhode Island	3.82	$921,000 min. size, rates .8%-16% (at $10M)
Vermont	5.41	$2.75M min. size, rates .8%-16%
New England Average	4.2	N/A
Oregon	4.77	$1M min. size, rates 10%-16% (at $9.5M)
New Jersey	3	$675,000 min. size, rates 4.8%-16% (on $10M)
United States Average	4.01	N/A

Connecticut's average increase in residents over 65 is below that of most of the region.

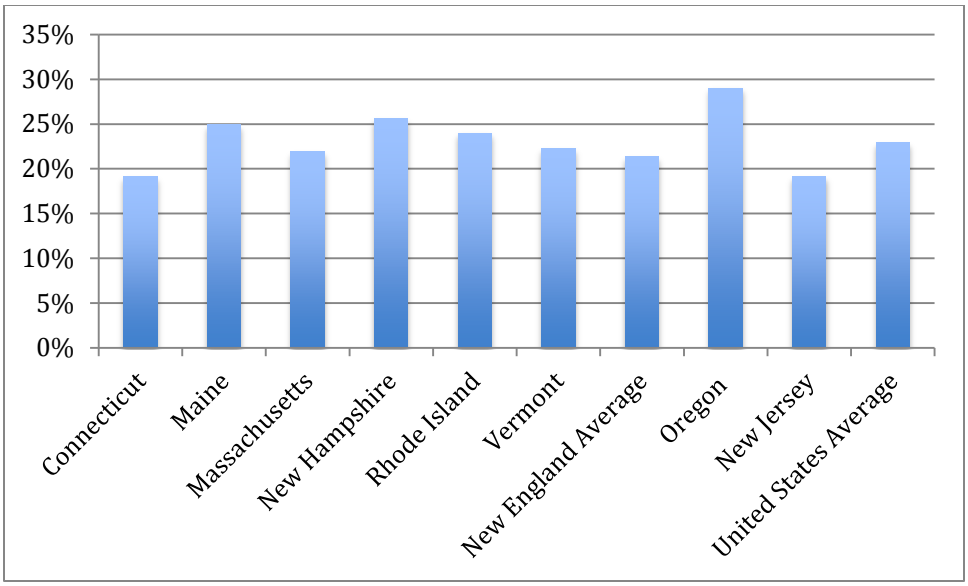
(6) Overall Adjusted Gross Income (AGI) of Taxpayers Over 65, Percentage Change Between 2012 and 2013



	Percentage change	Estate Tax Regime Type at time IRS data gathered (1/1/2013)
Connecticut	15.1	$2M min. size, rates 7.2% - 12% (at $10M)
Maine	15.03	$1M min. size, rates 8.0%-12% (at $10M)
Massachusetts	17.67	$1M min. size, rates .8%-16% (at $10M)
New Hampshire	18.6	**NONE**
Rhode Island	14.14	$921,000 min. size, rates .8%-16% (at $10M)
Vermont	13.18	$2.75M min. size, rates .8%-16%
New England Average	17.73	N/A
Oregon	17.33	$1M min. size, rates 10%-16% (at $9.5M)
New Jersey	15.1	$675,000 min. size, rates 4.8%-16% (on $10M)
United States Average	19.122	N/A

However, in terms of the increase in revenue gathered from such seniors, the disparity is far smaller. This suggests that the increase in individual taxpayers over-65 outside of Connecticut is driven more by the natural demographic change of an aging population than by any EI tax motivation.

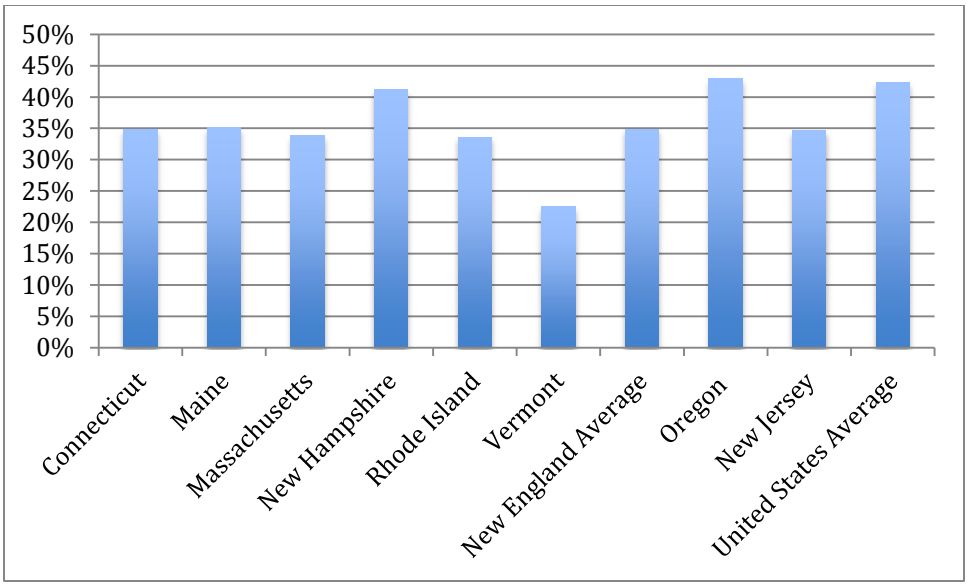
(7) Overall Number of Returns Filed by Taxpayers Over 65 and with Incomes above $200,000, Percentage Change Between 2012 and 2013



	Percentage change	Estate Tax Regime Type at time IRS data gathered (1/1/2013)
Connecticut	19.1	$2M min. size, rates 7.2% - 12% (at $10M)
Maine	24.9	$1M min. size, rates 8.0%-12% (at $10M)
Massachusetts	21.92	$1M min. size, rates .8%-16% (at $10M)
New Hampshire	25.59	**NONE**
Rhode Island	23.96	$921,000 min. size, rates .8%-16% (at $10M)
Vermont	22.26	$2.75M min. size, rates .8%-16%
New England Average	21.31	N/A
Oregon	29	$1M min. size, rates 10%-16% (at $9.5M)
New Jersey	19.12	$675,000 min. size, rates 4.8%-16% (on $10M)
United States Average	22.87	N/A

A final subgroup, individuals over 65 with incomes over $250,000, is also worth mentioning. As shown above, Connecticut's growth in such individuals lags behind other states in the region.

(8) Overall Adjusted Gross Income (AGI) of Taxpayers Over 65 and with Incomes above $200,000, Percentage Change Between 2012 and 2013



	Percentage change	Estate Tax Regime Type at time IRS data gathered (1/1/2013)
Connecticut	34.8	$2M min. size, rates 7.2% - 12% (at $10M)
Maine	35.07	$1M min. size, rates 8.0%-12% (at $10M)
Massachusetts	33.8	$1M min. size, rates .8%-16% (at $10M)
New Hampshire	41.14	**NONE**
Rhode Island	33.59	$921,000 min. size, rates .8%-16% (at $10M)
Vermont	22.5	$2.75M min. size, rates .8%-16%
New England Average	34.89	N/A
Oregon	42.93	$1M min. size, rates 10%-16% (at $9.5M)
New Jersey	34.664	$675,000 min. size, rates 4.8%-16% (on $10M)
United States Average	42.35	N/A

However, when one turns to the *income* generated by such individuals, this disparity narrows considerably. For example, the increase in Connecticut was roughly 35%, while the increase in (non-tax) New Hampshire was 40%. But the increase in the overall number of over-65 taxpayers in New Hampshire is *double* the same increase in Connecticut.

Once again, this suggests that New Hampshire's (relatively slight) advantage in income from high-income individuals over-65 is driven more by the natural demographic change of an aging population than by any EI tax motivation.

(9) The Garden State Parallel

Finally, it is striking to note that, across almost all of these metrics, Connecticut and New Jersey have nearly the precisely same data. This is a crucial result, because New Jersey's EI tax regime is substantially *more* progressive than that of Connecticut: as noted, the minimum size of taxable estates in the Garden State is only $675,000, considerably lower than Connecticut's minimum size of $2 million. Yet in considering the change from 2012 to 2013, the results are almost identical:

	% Change in Overall Returns	% Change in Overall AGI	% Change in Overall Returns, Income >200K	% Change in Overall AGI Income >200K	% Change in Overall Returns, Income > Age 65	% Change in Overall AGI Income > Age 65	% Change in Overall Returns, Income >200K & Age 65	% Change in Overall AGI Income >200K & Age 65
CT	-0.05	6.28	7.56	15.98	3	15.1	19.1	34.8
NJ	-0.05	6.28	7.57	15.98	3	15.1	19.12	34.664

Among other results, this suggests that Connecticut might be able to adopt New Jersey style EI taxes without adverse effect (see recommendations below).

IV. Policy Recommendations

Based on the foregoing analysis, this section offers three recommendations for possible shifts in Connecticut's EI regime:

Recommendation 1: Legislate with an understanding that state EI taxes work:

An initial recommendation, and one that is a premise of the other suggestions listed here, is that state EI taxes generally work well. As the academic literature and as the Connecticut-specific analysis shows, it appears that such taxes are not substantial drivers of outmigration, and that on balance they raise considerable revenue. Indeed, as the experience of states like New Jersey and Oregon make clear, it is possible for structures that seem even more progressive than Connecticut's to operate effectively. Accordingly, at a minimum, the current state EI taxes should be maintained, and there is plausibly room to make them even more progressive.

Recommendation 2: Reduce the minimum taxable estate size to New Jersey's level while lowering the rate of the estate tax:

Connecticut might change the structure of its estate tax to lower the threshold at which the tax kicks in while also lowering the rate of the tax itself. There are several reasons for such a shift. First, as noted above, New Jersey's experience suggests that a state comparable to Connecticut can viably lower the minimum estate size without causing massive outmigration. Indeed, such a shift would allow the tax to focus on a population less (potentially) mobile than the super-rich, suggesting even lower impacts on outmigration. Intuitively, such a shift would also be expected to make this revenue stream more consistent. Moreover, such a shift would have the added benefit of helping to decrease Connecticut's wealth gap – a disparity that helps perpetuate racial and other forms of inequality. At the same time, coupling the shift to a broader base with a lower overall rate would make the change more politically salable.

Recommendation 3: Consider progressive language linked to (potential) federal EI tax credits for states:

As noted in the historical material, prior to EGTRRA, all fifty states had estate tax systems linked directly to the federal estate tax, and which allowed the state to take advantage of such taxation. Today, the federal estate tax is in disarray. However, insofar as the prospect for federal estate taxes seems remote, now might be the most viable time to introduce language linked to (future) federal tax credits such that, in the event that such a regime does come into being, the state can immediately take advantage of it. As an example, the state might pass language saying that EI taxes will consist of *either* the current state EI regime *or* any federal EI tax credit regime, whichever is greater. Putting such language in place now might be a relatively easy way to ensure that, in the event progressive federal level taxation does occur, the state could benefit. That said it would be very important to consider the risks of such a proposal, namely that it might be amended in ways that would make it a vehicle to undermine Connecticut's system of state EI taxes.[39]

[39] *See* Norton Francis, "Back From The Dead: State Estate Taxes After The Fiscal Cliff," at 22, The Tax Policy Center, Nov. 14, 2014, available at http://www.urban.org/sites/default/files/alfresco/publication-pdfs/412694-Back-from-the-Dead-State-Estate-Taxes-After-the-Fiscal-Cliff.PDF ("Connecticut has a stand-alone tax structure with a top rate of 12 percent on taxable values over $10,100,000 and the first $3,500,000 is not taxed. There is a credit for gift taxes paid, which Connecticut levies. If the 2010 Act expires, the Connecticut estate tax may not be high enough to match the CSDT and Connecticut may not maximize the revenue from a return of the CSDT.").

Appendix A: States with non-dormant EI Taxes (as of 2015)

State	Tax Type (Estate, Gift, Etc.)	Exempt Estate Size	Rate Structure	Notes
NY	Estate	2,062,500	0.8% - 16.0%	Legislation in place means exemption will increase until it reaches federal level in 2019 (currently 5.35M)[40]
MD	Estate and Inheritance	1.5M	0.8% - 16.0%	Estate tax scheduled to increase exemption to match federal level in 2015. Maryland and New Jersey impose both types of taxes, but the estate tax is a credit against the inheritance tax, so the total tax liability is not the sum of the two, but the greater of the two taxes. Neither tax applies to bequests to lineal heirs.
CT	Estate	2M	7.2% - 12.0%	
D.C.	Estate	1M	0.8% - 16.0%	Exemption will increase to 2M in 2016, then planned to increase to federal level (currently 5.35M)
DE	Estate	$5,340,000 (equal to federal level)	0.8% - 16.0%	
MA.	Estate	$1,000,000	0.8% - 16.0%	
OR.	Estate	$1,000,000	0.8% - 16.0%	
HI.	Estate	$5,340,000	10.0% - 15.7%	
MN.	Estate	$1.4M	0.8% -	Increasing in annual increments until it reaches 2M in 2018. Also changes

[40]New York State's Estate Tax Changes, BNY Mellon Wealth Management, 2014, http://www.bnymellonwealthmanagement.com/Resources/documents/perspectives/new-york-estate-tax-change.pdf

			16.0%	rate.
NC	Estate	n/a	n/a	Phased out effective 2013.
RI.	Estate	$1.5M	0.8% - 16.0%	
IL.	Estate	$4M	0.8% - 16.0%	
NJ	Estate and Inheritance	$675,000	0.8% - 16.0%	MUTUALLY LOCKED DEDUCTION Maryland and New Jersey impose both types of taxes, but the estate tax is a credit against the inheritance tax, so the total tax liability is not the sum of the two, but the greater of the two taxes. Neither tax applies to bequests to lineal heirs.
VT	Estate	$2,750,000	0.8% - 16.0%	
ME	Estate	$2M	8.0% - 12.0%	
WA	Estate	$2,054,000	10.0% - 19.0%	
TN	Estate	$5M	5.5%-9.5%	Scheduled to be phased out.
IA	Inheritance Tax Only	Varies	5-15%, varies by relation to deceased	
KY	Inheritance Tax Only	Varies	4-16%, varies by relation to deceased	
PA	Inheritance Tax Only	Varies	4.5-15%, varies by relation to deceased	