

Budget Cuts, Taxes, and the Fiscal Crisis

Massachusetts has a budget deficit estimated at \$3 billion. How did this happen?

In the 1990s, rapid economic growth and a booming stock market created a temporary spike in state revenues. The legislature and the voters (through ballot questions) responded by repeatedly cutting the income tax and offering businesses sizable tax breaks. The campaign for the largest of these tax cuts argued that we could have a billion dollar tax cut “without cutting a single program.” Overall, taxes were cut by about \$3.7 billion.

During the same period, the legislature exhibited strong fiscal discipline on spending. Between 1991 and 2002 state spending dropped from 9.4% of personal income to 9.1%. By the year 2000, after a decade of cutting taxes and limiting spending, Massachusetts ranked 44th in the nation in total state and local taxes and fees as a share of personal income – only six states had a lower total burden.

If spending didn't cause the crisis, should cuts to essential services be the solution?

Slashing education, healthcare and other essential programs is not the only option.

- Restoring the income tax to the 5.95 percent rate in effect through most of the 1990s would raise just over a billion dollars and make most of the painful cuts unnecessary. Did the 5.95 percent tax rate of the 1990s constitute more of a crisis than the education and healthcare cuts now being proposed to pay for that tax cut?
- Closing corporate tax loopholes could restore up to \$400 million in state revenue. In 1968 the corporate income tax provided 16 percent of state tax revenue. Now it provides 4 percent. In 2000, one-third of the largest companies in the state paid less in income taxes than the average taxpayer. Closing tax loopholes by instituting combined reporting could generate up to \$200 million. Repealing specific corporate tax breaks, like single sales factor apportionment, could save up to another \$200 million.
- Increasing the sales tax one percentage point would generate \$700 million. As a share of personal income, Massachusetts now has the lowest sales tax of the 45 states that have a general sales tax. While the sales tax is generally regressive, Massachusetts does exempt food, rent, and most clothing and medical expenses.

There is no easy solution to the fiscal crisis. But it is important to look carefully at the causes of the crisis and to consider seriously all options for solving our problems.