

Connecticut's Dangerous Game: How the Nation's Wealthiest State Scared Off Businesses and Worsened Its Fiscal Crisis

By Andrew Mikula and Greg Sullivan



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Table of Contents

Executive Summary	4
The roots of Connecticut's tax crisis	4
Stagnant economy	7
Corporate exodus	13
Voting with their feet	14
No longer Taxachusetts	18
Conclusion	19



Executive Summary

Long the wealthiest state in the country in terms of per capita income, Connecticut today is suffering from a corporate revolt that has seen mainstays like General Electric and Alexion Pharmaceuticals move valuable headquarters operations out of state. Less visible but still very real has been a steady outflow of wealth to other states, with high earners increasingly moving to low-tax states like Florida and North Carolina. Connecticut's economic performance, in terms of growth of the number of millionaires in the Constitution State, is far below the national average.¹ Other economic indicators also point to trouble, including a stubbornly higher than average jobless rate. The state's billions of dollars of unfunded public employee pension obligations likewise illustrate the dire fiscal issues it faces.

There are a number of factors that contribute to the growing unease and turbulence in the Connecticut economy, generating headlines like the Atlantic's "What on Earth is Wrong with Connecticut?" and Governing's "The Fiscal Mess in America's Richest State." The Constitution State has lost 26,304 manufacturing jobs between 2008 and 2020, a drop of 14.1 percent, far greater than the U.S. drop of 5.3 percent over the same period.² Connecticut also ranked 49th among the states and D.C. in private sector wage gains and 48th in private sector employment gains between 2008 and 2020. It is one of only three states that have not recovered to pre-Great Recession employment levels, alongside West Virginia and Wyoming. The state's once-vaunted regional casino gambling monopoly is also eroding amid new competition from Massachusetts, Rhode Island and New York.

Connecticut's embrace of an aggressive tax policy to pay for ballooning government expenditures — including a sharp corporate tax rate increase — has been a major driver in the loss of bedrock employers. Higher corporate tax rates, combined with hikes in the personal income tax and, especially, the estate tax, also appear to be a factor driving away a growing number of the state's wealthiest residents.

The roots of Connecticut's tax crisis

Like the rest of the country, Connecticut has undergone some dramatic changes during the past quarter century. These changes have led to losses of major businesses and, from the start of the Great Recession through January 2020, an actual decline in jobs. The insurance and financial services sectors—pillars of the Connecticut economy—have taken hits as companies merge and consolidate, or as in the case of Aetna, move to what they perceive to be greener pastures.³ In addition to Aetna moving to New York City, in the past few years alone, Connecticut has lost General Electric and Alexion Pharmaceuticals to Massachusetts.

In recent decades, Connecticut has seen chronic instability and turmoil when it comes to state government spending and taxes. The last 29 years have been punctuated by a cycle of budget showdowns in Hartford between various governors and legislative leaders. While the faces and names change, the results have typically been the same: sharp tax increases to cover the rising cost of a host of government services, with ballooning public employee pension obligations and health care costs leading the way.⁴

That's not the way it was supposed to work out when Connecticut adopted the state's first income tax in 1991. Back in the 1980s, Connecticut had more in common with income tax-free New Hampshire, offering a lower-cost alternative to businesses and families than tax-and-spend states like New York and, at that time, Massachusetts.⁵

Connecticut had largely relied on a combination of a sales tax and corporate and capital gains levies to pay its bills, but revenue from all three plunged during the 1990–1991 recession, creating one of the worst state budget meltdowns in the country. When Gov. Lowell P. Weicker Jr., with help from Assembly and Senate Democrats, pushed through Connecticut's first income tax more than a quarter century ago, one aim was to provide a more solid base for state finances. Critics warned the new tax would beget more spending, but Weicker and other supporters of the income tax argued that plans for a constitutional cap on spending would provide the needed check.⁶

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The spending cap has since fallen by the wayside as Connecticut lawmakers have voted to raise the income tax four times in the last 20 years, in 2003, 2009, 2011, and again in 2015. The top rate has shot up 77 percent since 1991, from 4.5 percent to 6.99 percent.⁷ Behind the increases have been escalating public employee pension obligations and health benefits as well as payments on Connecticut's large debt load, which has now reached into the tens of billions. From 1991 to 2016, these government expenditures increased by 174 percent above the rate of inflation.⁸

Connecticut's budget and tax woes have intensified in the last few years, and former Gov. Dannel Malloy and state lawmakers increasingly targeted high earners and big companies to shoulder more of the burden. Faced with a \$3.3 billion budget shortfall in 2011, the state turned to an array of tax hikes to help cover the gap, with a particular emphasis on high earners and big companies. Along with raising the income tax, Gov. Malloy and state lawmakers doubled the surcharge tax for larger firms from 10 to 20 percent; rolled out a 7 percent luxury goods tax on yachts, jewelry, cars and clothes; and lowered the threshold for the estate tax from \$3.5 million to \$2 million.⁹

Gov. Malloy and lawmakers went back to the tax well in 2015 when they were again faced with a massive budget deficit, tapping the state's major corporations and the wealthy to close the gap. That year's budget hiked the top rate for individuals making over \$250,000 and couples more than \$500,000 from 6.7 to 6.9 percent, rising to 6.99 percent for single filers earning more than \$500,000 and couples pulling down more than \$1 million. Connecticut resident trusts and estates saw their taxes jump to 6.99 percent as well.¹⁰ There was also an increase in the relatively new luxury goods tax — covering everything from cars worth more than \$50,000 to clothing valued at over \$1,000 and up — from 7 percent to 7.75 percent.¹¹

Corporations didn't get off any easier. The 10 percent corporate tax surcharge was extended through 2021, while companies were prohibited from reducing their taxes by more than 50 percent through the use of tax credits, down from the previous 70 percent. In recent years, Connecticut has also expanded its pass-through entity tax base, effectively raised taxes on pass-through entity owners, and reduced tax credits for pass-through entities.¹² A decision to move towards a unitary reporting system in which major companies would have to pay taxes on operations beyond Connecticut's borders drew stern warnings from GE and Aetna, among other companies.¹³

After years of increases, Connecticut's state and local tax burden topped \$7,600 per capita by 2020, second in the country only to New York. In 2020, Connecticut also had one of the latest "Tax Freedom" days in the nation on April 25, three weeks later than Florida and nine days later than the country as a whole. The state's escalating array of tax hikes has not gone unnoticed by those at the top end of the income ladder.

According to USA Today rankings published in 2020, Connecticut ranked 2nd highest in total state/local tax burden per capita nationwide and in the top 10 in state-local tax burden as a percent of state income. Massachusetts, by comparison, ranked 6th and 25th highest, respectively (see Figure 1).¹⁴

While a budget showdown in Hartford again grabbed headlines in 2017, proposals for yet another income tax hike and for a levy on hedge funds went nowhere amid increasing pushback by the business community. In October 2019, revenue projections still showed that the status quo would produce billion-dollar budget deficits by fiscal year 2022, despite taking steps to increase revenue by over \$2.5 billion during the 2019 legislative session.¹⁵ During the COVID-19 pandemic, Connecticut has relied largely on its Rainy Day Fund to balance its budget, an unsustainable strategy that does nothing to mitigate a billion-dollar rise in fixed costs.¹⁶ Left to foot the bill for Connecticut's fiscal meltdown on multiple fronts, major employers and some of its wealthiest families and individuals have been heading for the exits.

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Figure 1. List of states by state & local tax burden, 2020¹⁷

State	State & local tax burden as a share of state income	Rank	State & local tax burden per capita	Rank
New York	13.8%	1	\$9,059	1
Connecticut	10.6%	10	\$7,655	2
New Jersey	10.7%	7	\$6,947	3
North Dakota	12.7%	2	\$6,689	4
Hawaii	12.5%	3	\$6,643	5
Massachusetts	9.6%	25	\$6,550	6
Maryland	10.4%	13	\$6,293	7
California	10.3%	14	\$6,196	8
Minnesota	11.2%	6	\$6,151	9
Vermont	11.6%	4	\$6,029	10
Illinois	10.7%	8	\$5,772	11
Rhode Island	10.6%	9	\$5,552	12
Washington	9.1%	30	\$5,328	13
Maine	11.4%	5	\$5,309	14
Pennsylvania	9.7%	22	\$5,155	15
Nebraska	10.1%	17	\$5,117	16
Iowa	10.5%	11	\$4,983	17
New Hampshire	8.4%	41	\$4,905	18
Delaware	9.7%	23	\$4,884	19
Wisconsin	9.9%	19	\$4,880	20
Colorado	8.8%	33	\$4,869	21
Virginia	8.7%	36	\$4,812	22
Oregon	9.8%	21	\$4,740	23
Wyoming	8.3%	44	\$4,679	24
Ohio	10.0%	18	\$4,665	25
Kansas	9.5%	27	\$4,643	26
Nevada	9.6%	26	\$4,504	27
Louisiana	9.9%	20	\$4,350	28
South Dakota	8.6%	38	\$4,262	29
Michigan	9.1%	31	\$4,209	30
Texas	8.7%	35	\$4,170	31
New Mexico	10.4%	12	\$4,110	32
Alaska	7.2%	50	\$4,089	33
Utah	9.2%	29	\$4,048	34
Arkansas	9.6%	24	\$3,986	35
North Carolina	9.0%	32	\$3,976	36
West Virginia	10.2%	15	\$3,942	37
Montana	8.6%	39	\$3,897	38
Kentucky	9.5%	28	\$3,895	39
Indiana	8.6%	37	\$3,889	40
Missouri	8.4%	43	\$3,842	41
Georgia	8.4%	40	\$3,741	42
Idaho	8.8%	34	\$3,704	43
Mississippi	10.1%	16	\$3,674	44
Florida	7.6%	48	\$3,638	45
South Carolina	8.4%	42	\$3,535	46
Oklahoma	8.1%	47	\$3,534	47
Arizona	8.2%	46	\$3,485	48
Tennessee	7.6%	49	\$3,416	49
Alabama	8.3%	45	\$3,359	50

Stagnant economy

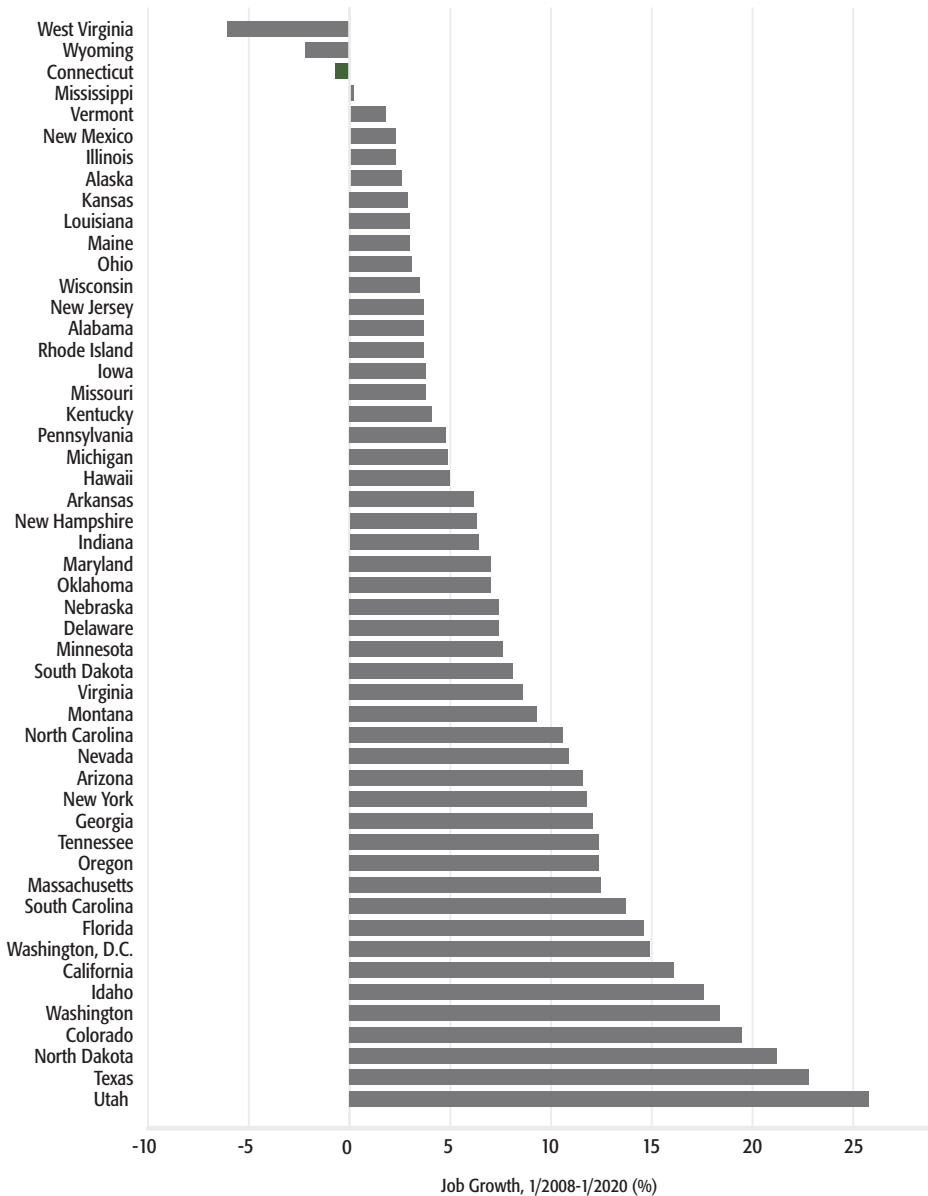
Like many states in the Northeast, Connecticut has been adversely impacted by some significant long-term economic trends. The Constitution State has seen a steady drop in manufacturing jobs amid growth in lower-paid sectors like health, education and tourism. It is an expensive state to live in, with some of the highest housing costs in the country.

Connecticut's economy has dramatically underperformed the nation and New England over the past decade, a period of near constant state budget emergencies in Hartford followed by sharp tax hikes. It is part of a larger trend, with Connecticut's recovery from the Great Recession markedly slower than the country as a whole and slower than its more economically dynamic neighbor to the north, Massachusetts.

Between the pre-Great Recession employment peak in January 2008 and January 2020, only three states have failed to restore employment to pre-recession levels: Connecticut, West Virginia, and Wyoming. Unlike the post-recession struggles of West Virginia and Wyoming, however, Connecticut's stagnant economy is harder to link to a heavy reliance on energy production and natural resource extraction. Connecticut had 11,800 fewer seasonally-adjusted jobs in January 2020 than in January 2008, and the biggest contributors to that deficit are the manufacturing, financial services, and retail sectors.

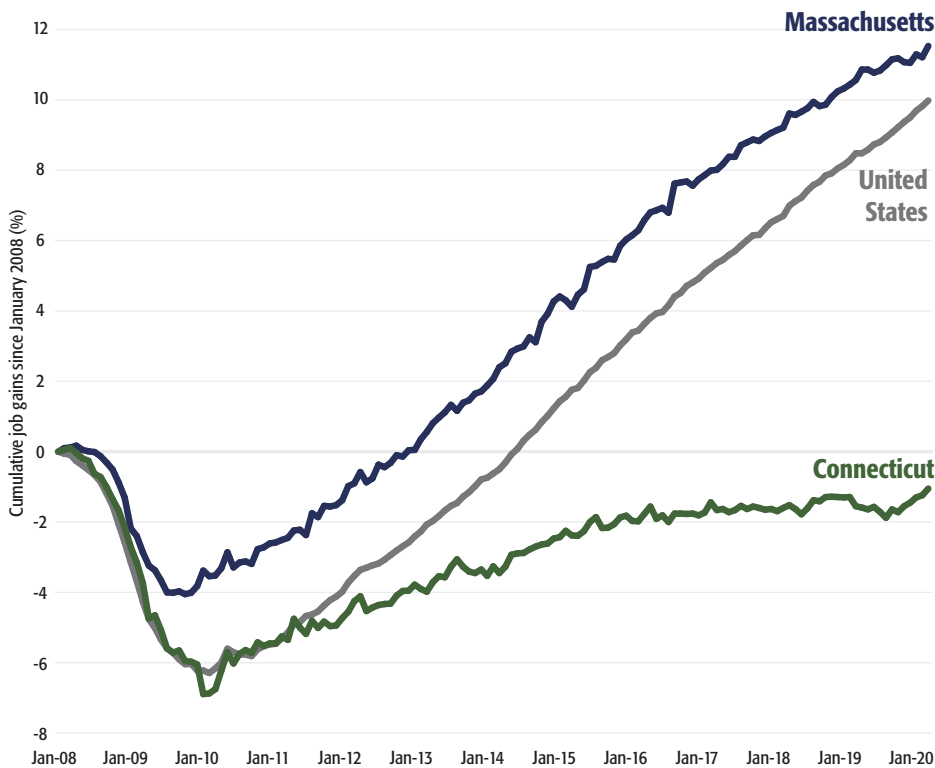
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Figure 2. Non-farm employment growth rate by state, January 2008 – January 2020¹⁸



A July 2017 report from Connecticut state comptroller Kevin Lembo predicted the state would recover its jobs lost during the Great Recession in “a little over two years.”¹⁹ Instead, Connecticut’s recovery stalled, and after Lembo’s report was published, the state continued to lose jobs on net through the summer of 2019. To put this in a national perspective, U.S. employment had surpassed pre-Great Recession levels by May 2014. Figure 3 compares recession job recovery in Connecticut and Massachusetts to the U.S. as a whole, showing that in January 2020 the U.S. had 10 percent more seasonally-adjusted nonfarm jobs than it did in January 2008, while Connecticut had 1 percent fewer jobs.²⁰ Massachusetts comfortably outpaced the national average, with 11.5 percent job gains over the period.

Figure 3. Cumulative nonfarm employment gains in the U.S. and Connecticut, January 2008 – January 2020²¹

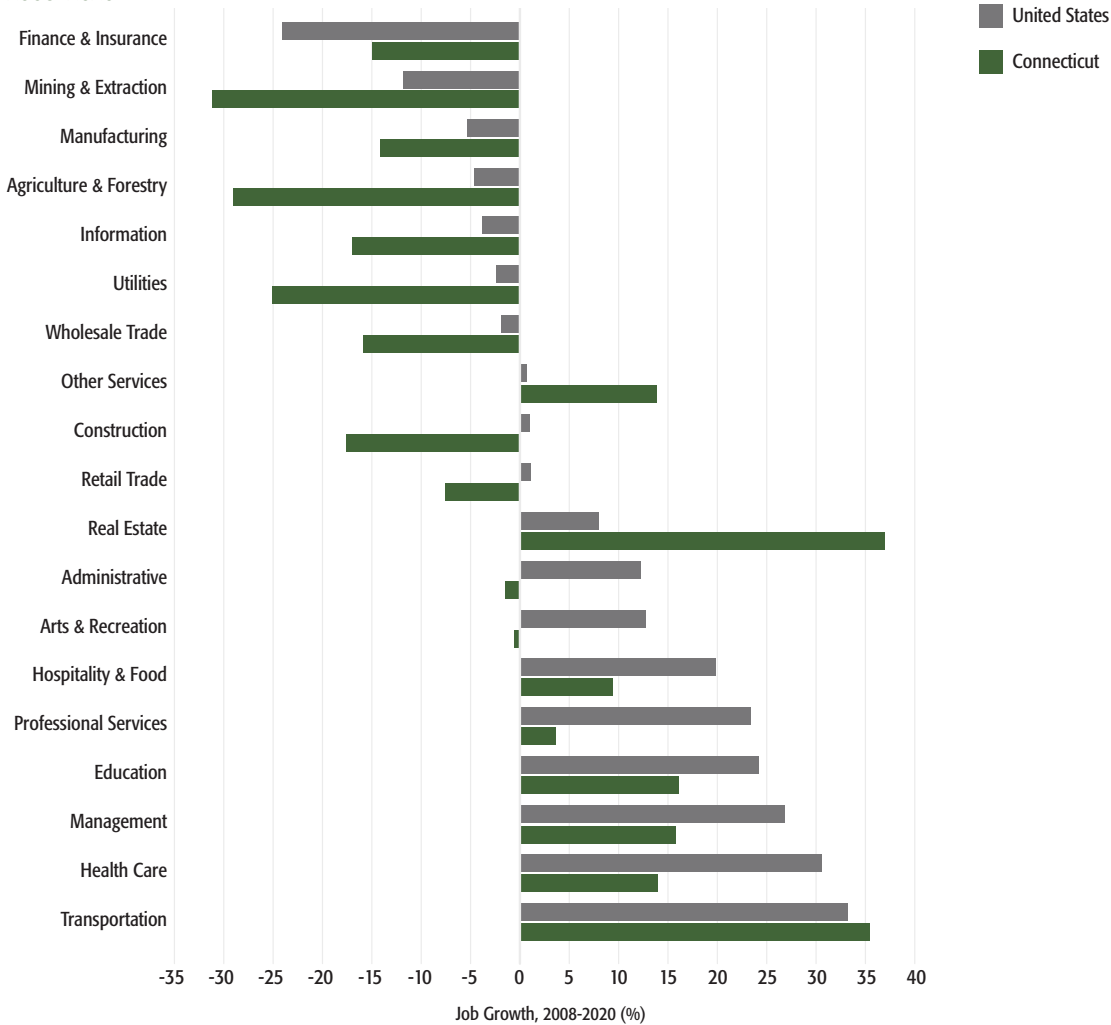


Meanwhile, it’s difficult to pin this economic stagnation on any one industry. Between 2008 and 2020, Connecticut underperformed the U.S. in 14 of the 18 private industry sectors classified by the North American Industry Classification System (NAICS). Connecticut suffered double-digit job losses in eight of those sectors, including financial services (-14.9 percent), manufacturing (-14.1 percent), construction (-17.6 percent), and utilities (-25.1 percent), among others (see Figure 5). Still, job losses in financial services, a well-represented sector in Hartford and statewide, were not quite as severe as in the nation as a whole.

Another useful measure of the dissonance between Connecticut and the rest of the country in terms of economic performance is private sector compensation growth. Connecticut ranked 49th among the states in private sector wage gains from 2008 to 2020, with private sector paychecks increasing just 19.1 percent in the Constitution State compared to 34.2 percent in the U.S. as a whole (see Figure 6).²² By comparison, Massachusetts added 41.0 percent, beating the national average. Connecticut also underperformed the U.S. in wage growth in 14 of the 18 NAICS sectors.

Connecticut ranked 49th among the states in private sector wage gains from 2008 to 2020, with private sector paychecks increasing just 19.1 percent.

Figure 4. Private Sector Job Growth by NAICS Sector in the United States and Connecticut, 2008–2020²³



It is important to note that the new jobs being created in the Constitution State are also not as high-paying as the ones it has been losing. A 2016 report by the Connecticut Commission for Economic Competitiveness found that jobs added by the state's new growth industries — health care, food service and education — had an average annual pay of \$54,018. More remunerative fields, like IT, manufacturing and construction, where wages average \$75,246, are shedding jobs.²⁴

According to the State Economic Competitiveness Index series published by the American Legislative Exchange Council (ALEC), Connecticut's economic outlook ranked 32nd among the states in 2009 (with 1 being best and 50 worst).²⁵ By 2020, its rank had slipped to 40th. In its most recent report, ALEC cited Connecticut's sluggish GDP growth and persistent domestic out-migration as especially alarming.²⁶ It also ranked Connecticut as the single worst state in terms of economic performance between 2008 and 2018. The same report found that a 2019 tax increase threatened to decrease Connecticut's economic outlook rank from 40th to 44th.²⁷

Repeated budget crises and tax hikes don't just result in a sluggish economy and job losses. Homeowners are also taking a hit. Connecticut ranked dead last among the 50 states and Washington, D.C. in house price appreciation between 2012 and 2020 (see Figure 8).²⁸ In Fairfield County, which is well-known for its high concentration of wealthy individuals and large corporations, home values remained 18 percent below their 2006 peak as of 2019.²⁹

A 2019 tax increase threatened to decrease Connecticut's economic outlook rank from 40th to 44th.

Figure 5. Private sector wage growth by state, 2008–2020³⁰

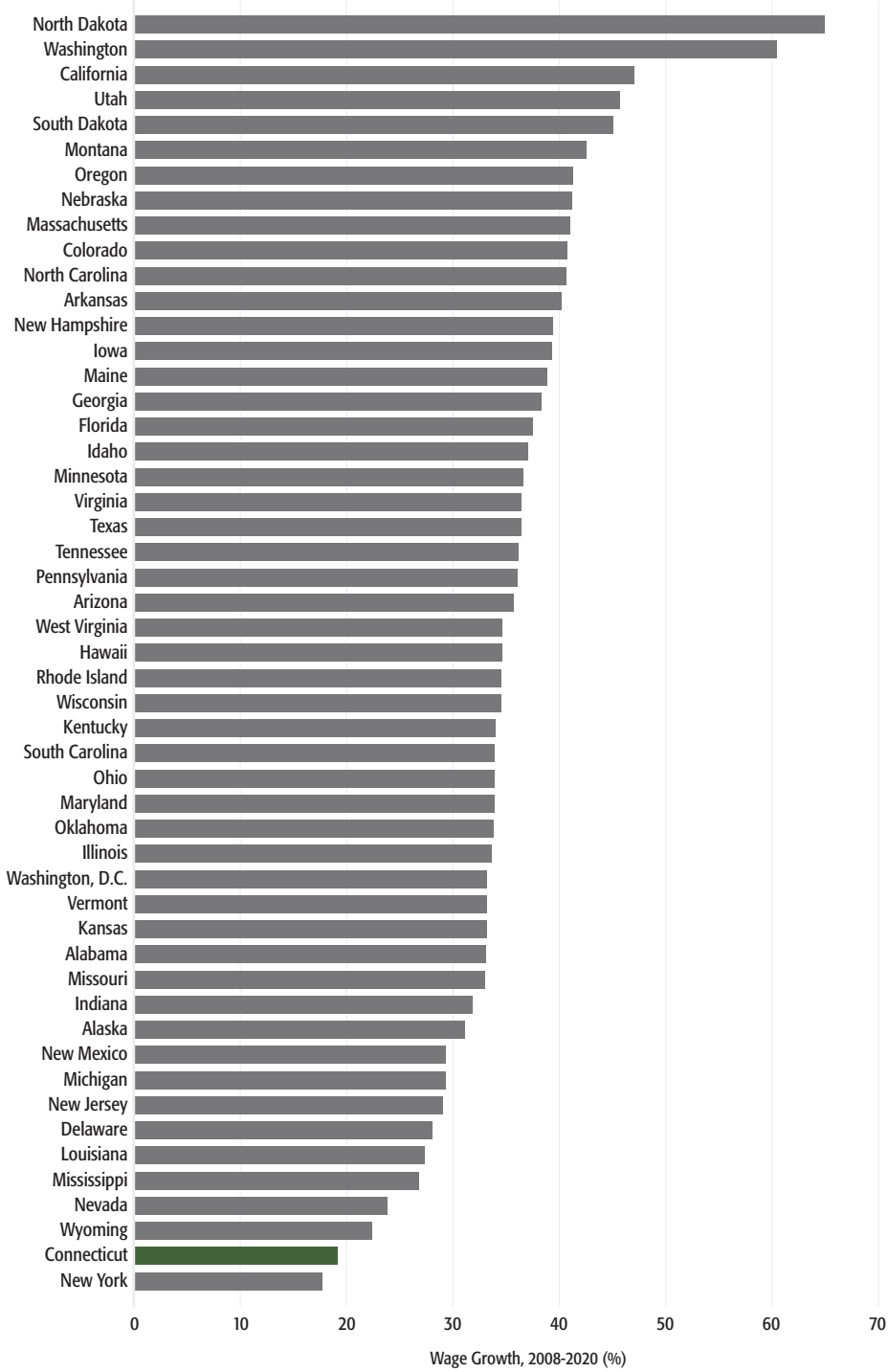
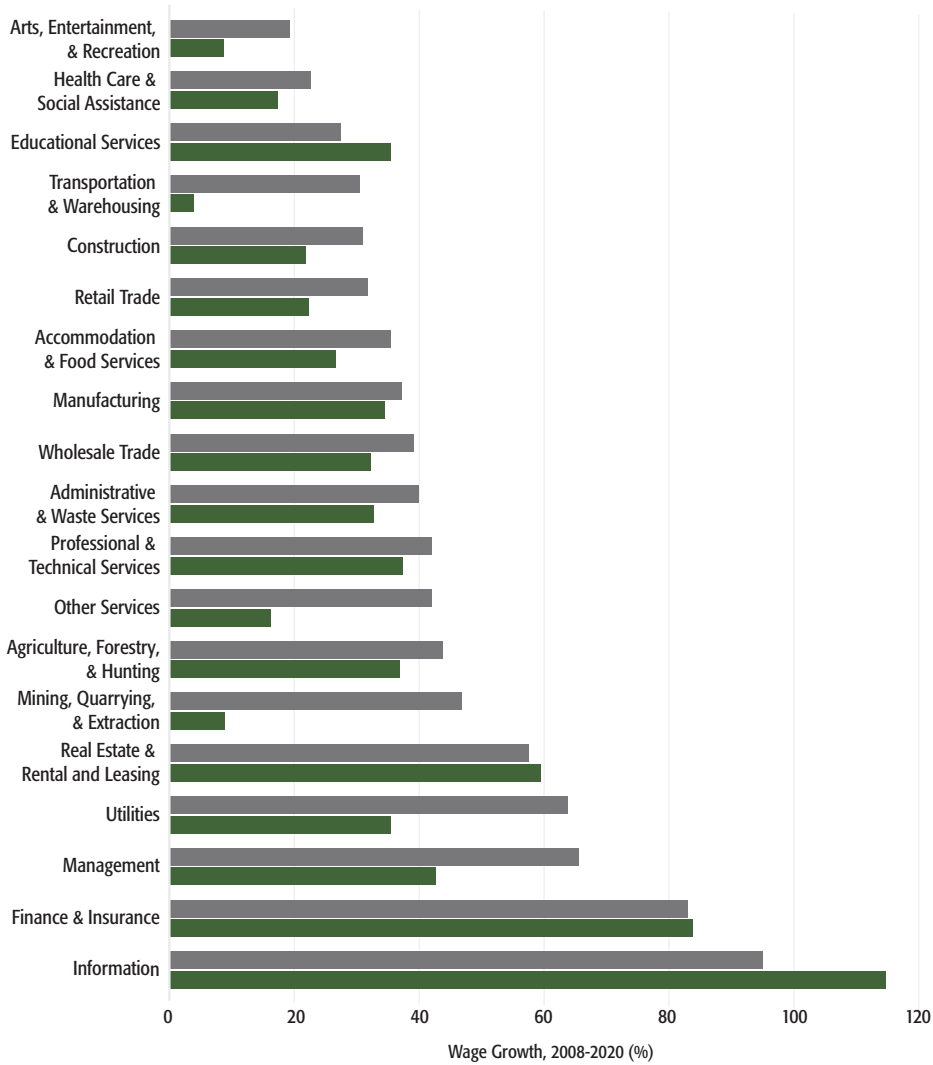
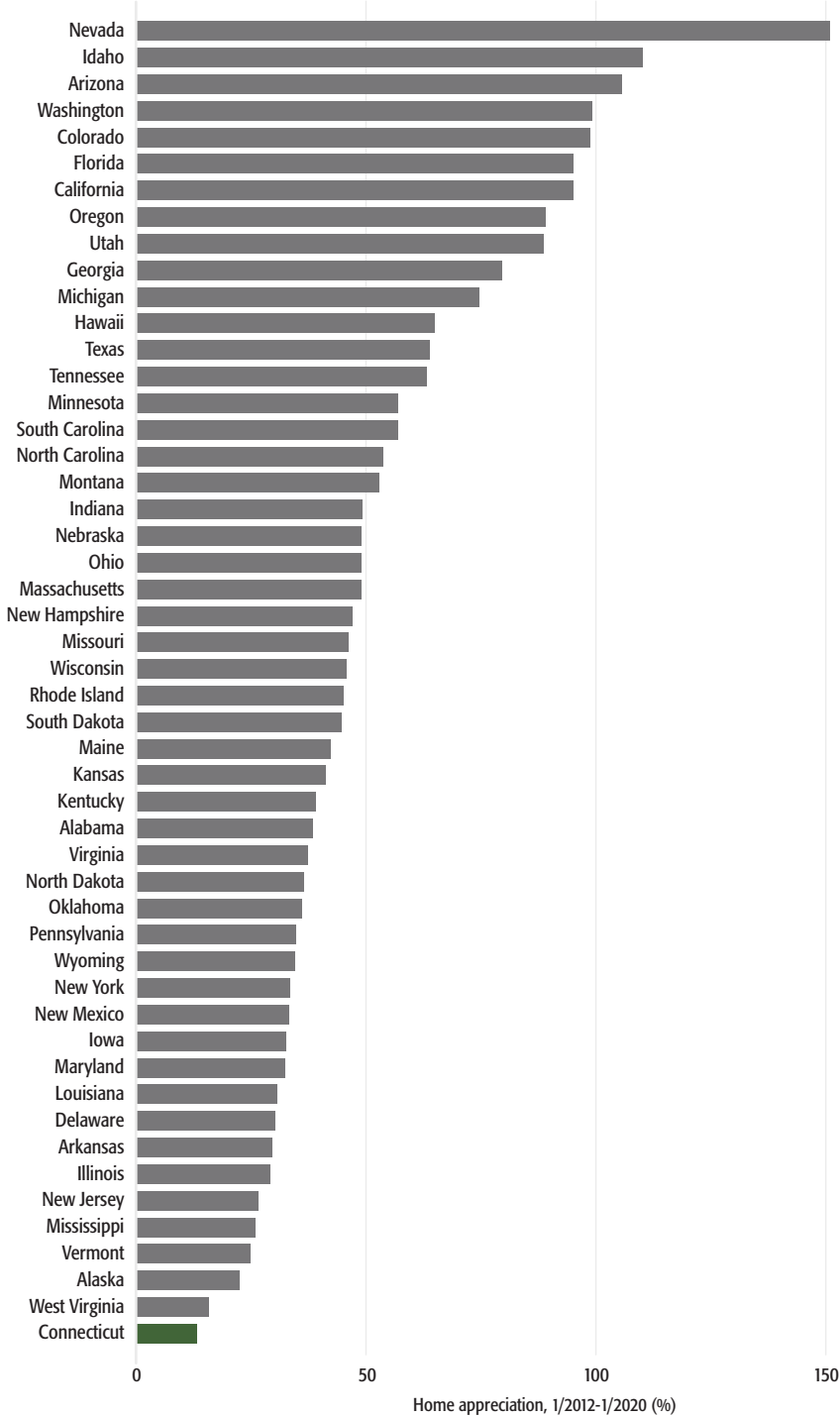


Figure 6. Private Sector Wage Growth by NAICS Sector in the United States and Connecticut, 2008–2020³¹



The economic damage done by Connecticut’s perennial budget deficits have apparently been compounded by the state’s decision to deal with them by repeatedly hiking taxes, according to economist Nicholas Perna. “Deficits are not just corrosive to confidence in the business climate, but eliminating them through taxes or spending cuts is a drag on the economy,” Perna noted in an interview with the CT Mirror.³²

Figure 7. Home value appreciation by state, Q1 2012 to Q1 2020³³

Looking ahead, Connecticut's outlook is clouded by high taxes and high debt. The state has the 6th highest property taxes and 12th highest personal income taxes in the country.³⁴ The Constitution State is one of just 11 states to have its own estate tax, and Connecticut's base estate tax rate of 10 percent is tied for second highest in the nation.³⁵ The state's budget for fiscal years 2020 and 2021 includes hundreds of millions of dollars of tax hikes and revenue grabs, all while burdening the business community with minimum wage increases and paid family and medical leave obligations. The General Assembly also called for an exploratory study of a payroll tax on employers, which could be implemented as early as 2021.

Meanwhile, consumers have to contend with an additional 1 percent tax on restaurant meals and expansions of the state sales tax to cover motor vehicle parking, dry cleaning, interior design services, and other activities.³⁶ Especially given the state's two-year budget process, the pandemic has set up Connecticut for another harsh budget season again in the spring of 2021.

Corporate exodus

Faced with a sluggish economy and constant turmoil over the state budget and taxes, some of Connecticut's top companies have and continue to move to other states. This corporate exodus threatens to further exacerbate the state's already serious tax and budget woes.

General Electric has been at the forefront of this outmigration after its 2016 decision to move its headquarters to South Boston's booming waterfront. GE once promised to employ up to 800 people, including many highly paid top executives, in South Boston, but recent estimates pin the number at closer to 250.³⁷

Despite this disappointing result, there isn't much of a silver lining for Connecticut, which simply failed to maintain the friendly business climate and political favoritism that GE had come to expect.³⁸ While the tax incentives used to lure GE to Boston rightfully remain controversial, by 2016 Massachusetts was clearly in a better position than Connecticut to pour money into corporate tax breaks after gross public debt had fallen for five straight years as a percentage of GDP. By contrast, gross public debt rose in Connecticut as a share of GDP every year from 2007 to 2020.³⁹

GE's exit has only exacerbated this debt crisis. General Electric once paid roughly \$1.9 million a year to the Town of Fairfield alone, and hundreds of well-paid GE executives no longer pay Connecticut income taxes after the company's move to Boston.⁴⁰

Still, perhaps the biggest damage from GE's exit is to Connecticut's once solid reputation as a good place to do business. Connecticut's failure to hang onto the crown jewel of its corporate community — or at least to make a reasonable show of responding to GE's concerns — has helped make the Constitution State a poster child for states seemingly hostile or indifferent to the concerns of business, sparking negative business press coverage.

GE's move has also paved the way for defections by other companies that are unhappy about the direction of Connecticut's tax and budget policies. Aetna's public outcry over state taxation may have been even more unsettling given the company's roots in Connecticut that go back to 1853. While most of the insurer's employees remain in Hartford, the loss of its top executives to New York still entails millions of dollars in lost income tax revenue.⁴¹

Even so, Aetna offered a warning, tying the issue of whether it will keep a substantial number of employees in Connecticut over the long term to the state's economic health and the ability of political leaders to put state finances on a "sound financial footing."⁴²

Later in 2017, Alexion Pharmaceuticals joined the exodus, announcing plans to move to Boston by mid-2018, despite having to pay back a \$20 million loan from the State of Connecticut and a \$6 million grant.⁴³ The company is now located just a 10-minute walk from GE's South Boston headquarters.

It would be hard to argue that no one saw this corporate rebellion brewing. GE and Aetna were out front in warning Connecticut's political establishment about the potential consequences of its seemingly endless cycle of budget crises followed by tax hikes. With a \$700 million tax hike in the works, Aetna, Travelers and GE all released statements on the same day in June 2015 warning Governor Malloy and legislators of the potential consequences of moving forward. GE warned it would "seriously consider whether it makes any sense to" to remain in Connecticut," while Aetna made clear "such an action will result in Aetna looking to reconsider the viability of continuing major operations in the state."⁴⁴

Connecticut lawmakers passed the tax package anyway. One senator argued that the increases, which supporters argued would be used to pay for overhauls to the state's transportation system, signaled "a brighter day" ahead.⁴⁵

Gross public debt rose in Connecticut as a share of GDP every year from 2007 to 2020.

The plan included a “unitary tax” requiring companies to pay taxes on their subsidiaries and operations in other jurisdictions, not just Connecticut. With its global footprint, GE had been particularly vocal about its concerns about that part of the tax increase package.⁴⁶

Voting with their feet

It is not just Connecticut’s leading corporations that are reconsidering whether to stay in the Constitution State. Some of the state’s wealthiest families and individuals have also been voting with their feet.

Most wealthy individuals don’t have the megaphone of a large, corporate organization from which to broadcast their displeasure over state budget and tax policy changes. For myriad reasons, high net worth individuals may also be loath to take actions that draw attention to their status or inject themselves into volatile and contentious public debates.

However, in 2014, the IRS for the first time began to report “Gross-Migration File” data, which tracks changes in address reported on income tax returns. The data tracks both “inflows”— taxpayers moving into a particular state or county — and “outflows,” or those leaving. The returns are also grouped by age and adjusted group income (“AGI”) in tiers ranging from \$0 – \$10,000 to \$200,000 and up.

The data affords researchers the opportunity to study the inward and outward state migration of individuals with relatively high incomes. It does, however, have its critics, who note that just because someone moves out of state doesn’t mean the job and taxable income they are leaving behind is lost, arguing that someone else will be hired to fill the position.

Critics have also taken aim at studies arguing that state tax rates are the primary reason why some states are losing population, especially among wealthier residents. There are obviously many factors driving migration from some states and towards others, including a preference for the sunnier climes of Florida and Texas by retirees from the chillier Northeast. Housing costs and economic factors are also important, especially if opportunities for advancement and profit are more abundant elsewhere.

Yet it would be disingenuous to say that tax rates and additional levies like estate and inheritance taxes play no role in why some states are losing population to others that don’t have income or estate taxes. That is especially true in the case of Connecticut, which has lost a significant number of its wealthiest citizens during a time of rising tax rates combined with one of the most lackluster economic performances in the country.

In 2018 alone, Connecticut lost over \$1.2 billion in net AGI outmigration. On a per capita basis, only Washington D.C., New York, Illinois, Alaska, and New Jersey lost more.⁴⁷ Over the period 2012–2018, net AGI losses from interstate movement totaled \$12.3 billion in the Constitution State, more than Massachusetts’ corresponding figure of \$8.5 billion despite the fact that Connecticut has about half of Massachusetts’ population.

Overall, 27,537 taxpayers with an AGI of at least \$200,000 (hereafter, “high-income taxpayers”) moved out of Connecticut between 2012 and 2018, far outpacing the 20,174 who moved in. Tellingly, the average annual income of the high-income taxpayers who moved out, \$765,958, well exceeds the average income of those who moved in, \$634,364. While migration created a decline in AGI in every income bracket tracked by the IRS from 2012 to 2018, top earners made up over two-thirds of Connecticut’s tax revenue migration losses over the period, a product of their disproportionate wealth and high out-migration rates (see Figure 9).

On a per-capita basis, Connecticut’s net migration of AGI among high-income taxpayers was second worst in the country from 2012 to 2018, with only Washington, D.C. seeing more taxable income flee.⁴⁸ Over this period, Connecticut received an average of 121,749 tax returns per year from taxpayers with an AGI of \$200,000 or more. Its net AGI out-migration of taxpayers in this income category was a staggering \$8.29 billion, representing an average AGI loss of \$765,958 for every high-income taxpayer who left. While Connecticut and D.C. were losing net AGI due to out-migration of high-income taxpayers, many states, led by

In 2018 alone, Connecticut lost over \$1.2 billion in net AGI outmigration.

Florida, had net positive gains in AGI among high-income taxpayers (see Figure 10). In just seven years, 122,341 high-income taxpayers moved to Florida, adding \$3,244 of taxable income to Florida's AGI for each resident the state had in 2012.

The decision by some of the state's wealthiest families to move elsewhere has contributed to a decline in tax revenue that has only helped deepen Connecticut's latest budget crisis. And state officials have announced public recognition of this issue. Taxes paid by the state's top 100 taxpayers plunged by 45 percent from 2015 to 2016 alone, adding up to a \$200 million hit.⁴⁹ In 2016, the wealthiest 3 percent of taxpayers in Connecticut were still responsible for 41 percent of income tax payments.⁵⁰

In 2010, there were 11 Connecticut billionaires on the Forbes 400 list of the wealthiest Americans.⁵¹ By 2020, that list had shrunk to five.⁵² Of the previous decade's 11, four had moved to Florida and one had died.⁵³ Meanwhile, two had fallen off of the list for financial reasons and another, logistics entrepreneur Bradley Jacobs, had joined the list for the first time. The four who fled to Florida, including Paul Tudor Jones, Edward Lampert, Thomas Peterffy, and C. Dean Metropoulos, had a combined net worth of \$27.5 billion as of November 2020. While calculating how much each would have paid in taxes is difficult, as many of the details of each man's investment income and salaries are not public, the stock market often nets them tens of millions of dollars every day, implying a nine-figure loss of revenue for the State of Connecticut.⁵⁴

In 2010, there were 11 Connecticut billionaires on the Forbes 400 list of the wealthiest Americans. By 2020, that list had shrunk to five.

Figure 8. Net AGI loss due to migration in Connecticut by income group, 2012–2018

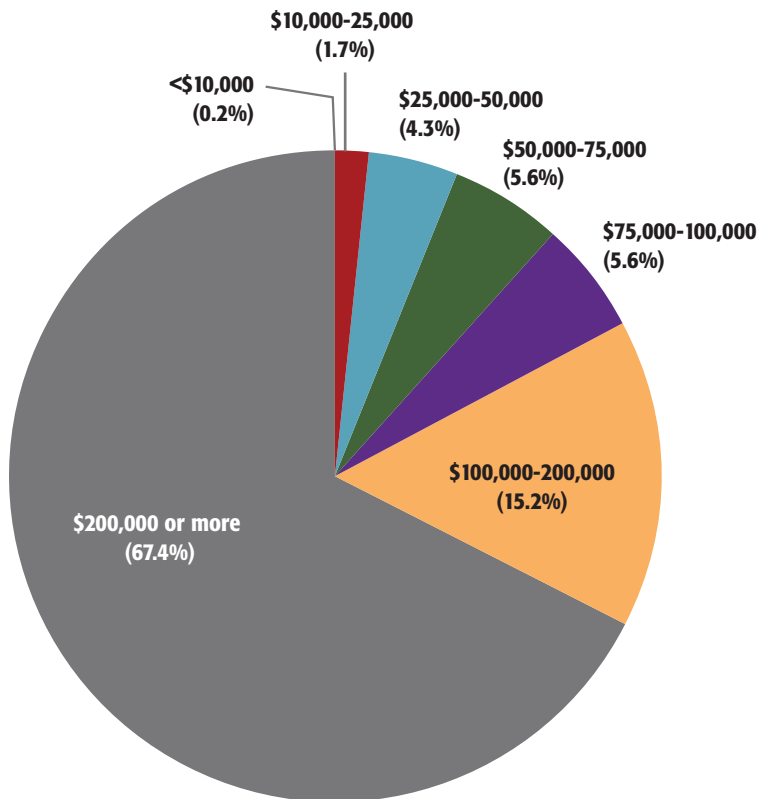
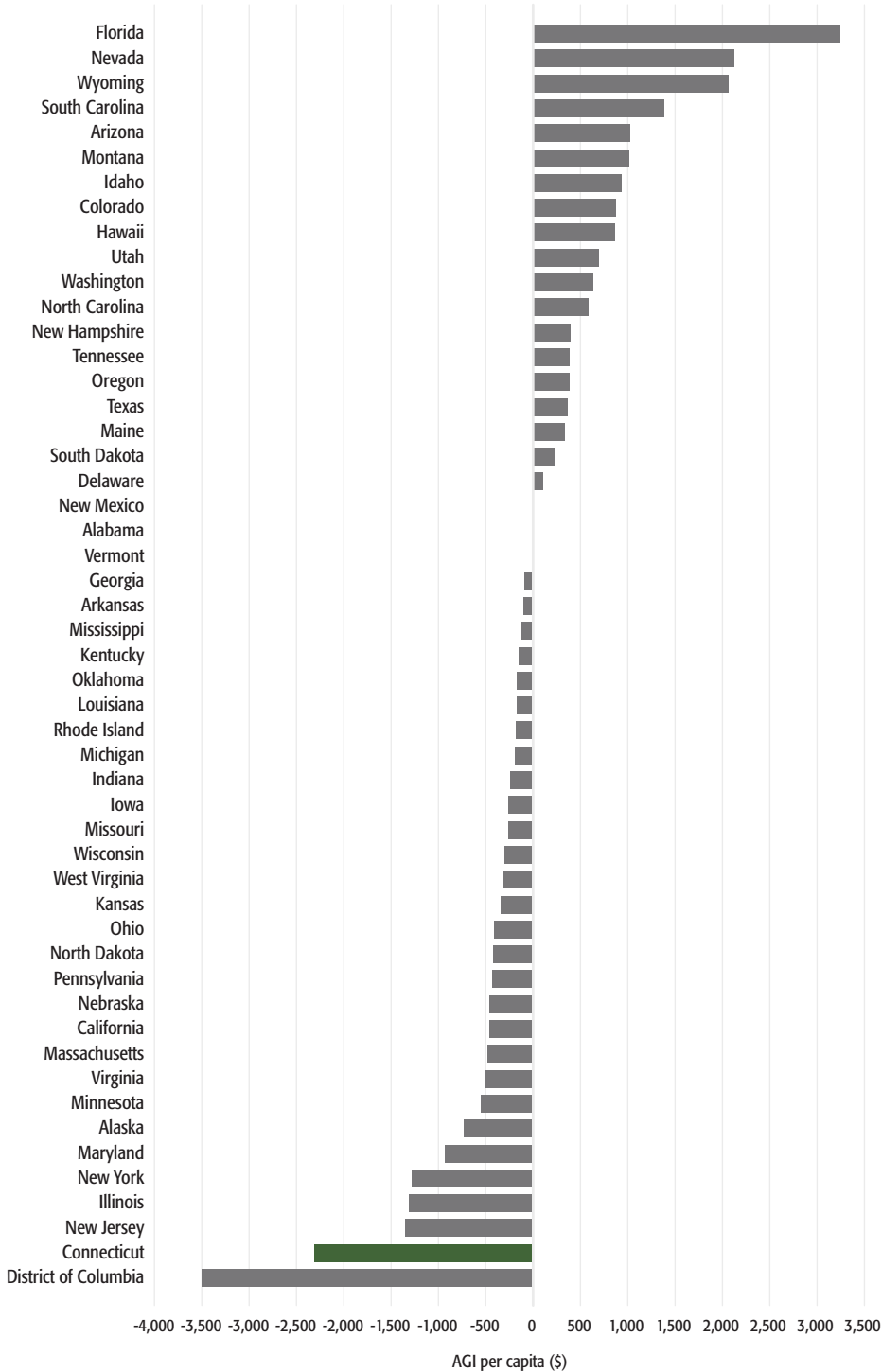


Figure 9. Per capita net AGI loss due to migration of high-income taxpayers by state, 2012–2018



Beyond out-migration of high-income residents, a number of additional factors may be fueling the drop off in taxes paid by Connecticut's wealthiest residents. State revenue officials point to a decline in the hedge fund industry, for example.⁵⁵ And while migration rates of the wealthy are often relatively low, Kevin B. Sullivan, commissioner of the Connecticut Department of Revenue Services, admitted in 2016 that "five or six of the highest earners could have a measurable impact on the revenue stream." The state's over-reliance on the wealthy to fill state coffers has even led it to track how much some of its most affluent individuals should be paying in taxes each quarter.⁵⁶

Moreover, Connecticut's wealthiest families may be taking other measures short of completely relocating to protect their income as the state repeatedly raises rates. Stories abound of multi-millionaires who have changed their tax domiciles to Florida, despite continuing to operate businesses in Connecticut or New York City.⁵⁷ After a brief lag, it seems that efforts to avoid taxation have caught up with tax hikes. The amount of taxes paid by the top 100 jumped after rates climbed in 2011 and 2015, only to fall again the following years, state revenue officials have said.⁵⁸

It's not just about the income tax, either. The wealthiest taxpayers also pay close attention to estate and gift taxes, which can fall heavily on those in the highest tax brackets. Connecticut is one of a dwindling number of jurisdictions with an estate tax and the only state with a gift tax.

Twelve states still have an estate tax in 2020, down from 15 in 2015 after Tennessee, Delaware, and New Jersey all abolished the levy.⁵⁹ Several other states have decided to raise their thresholds for applying the tax, with New York notably upping it to \$5.25 million.⁶⁰

But under pressure to meet the rising cost of ever-growing public employee pension obligations, Connecticut has moved in the opposite direction. During the 2011 budget crisis, the state lowered the threshold for its estate tax, which tops out at 12 percent, from \$3.5 million to \$2 million.⁶¹ Four years later, amid another budget showdown, state lawmakers lifted a \$12,500 cap on probate fees, while estates over \$2 million had court fees raised to 0.5 percent, enough so probate costs topped \$1 million for some large estates.⁶²

While Connecticut is currently set to raise its estate tax threshold to the federal level of \$11.6 million by 2023, the economic damage from its era of recklessness has already been done.⁶³ Connecticut's decision to double down on the estate tax, along with its income tax hike, has arguably been a significant factor contributing to the outflow of wealthy families and their assets since 2013. A 2008 study by Connecticut revenue and budget officials zeroed in on the reasons why residents and retirees were leaving the state. More than half the estate planners surveyed for the study reported having clients who changed their main residence from Connecticut or moved to another state altogether "primarily" due to the estate tax.⁶⁴

The study found that the average estate of those who left Connecticut was \$7.5 million, which would have equated to \$705,200 in potential estate taxes, while their average taxable income was \$446,000. This resulted in a loss to the Connecticut treasury of nearly \$22,000 in income taxes from each family who left.⁶⁵ The top four destinations were Florida, New Hampshire, Arizona and North Carolina, none of which have estate taxes. The top four concerns of clients who moved out of Connecticut were the state's income tax, its estate tax, the New England climate, and already spending part of the year out of state.⁶⁶

The study by Connecticut revenue officials also noted it's not that hard to change your principal address for tax purposes given the options opened up by modern travel and the personal computer and the internet. It can be as simple as listing a second home as a main residence.

The ease with which Connecticut's highest earners are able to side-step estate taxes and the state's 12 percent gift tax, another levy unpopular with the wealthy, were highlighted in an op-ed by David DeLucia, a retired executive living in Darien after a long and successful career on Wall Street.⁶⁷ DeLucia notes that all but one of his "super wealthy" friends in Connecticut have since moved to Florida. He is particularly irked by Connecticut's gift tax, noting it is the only state with such a fee. After a lifetime of paying taxes, DeLucia feels he has paid his fair share and then some. "Wealthy people have options, especially mobility," DeLucia writes. "If I sell my Connecticut home, move to any other state and then make gifts of my wealth to my heirs, I save them millions of dollars. My super wealthy friends call this the 'free move.' You can move out of Connecticut and the gift tax savings more than offsets the cost of the move and the new home purchase. Why wouldn't anyone do this?"

When the wealthy leave, the state doesn't just lose out on the income taxes they would

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have paid. Their spending on “expensive cars, big homes, expensive jewelry ... fancy restaurants” also moves with them, not to mention wages paid to “landscapers, plumbers, electricians, etc.,” DeLucia argues. “Connecticut politicians seem wedded to their simple strategy of, “Let’s keep raising taxes on the remaining corporations and the wealthy so they can all pay their fair share,” DeLucia writes. “This one-trick pony only works for so long and, I might add, when you put on too much weight, even a strong pony collapses.”

This outmigration of the wealthy is part of a national trend that is seeing the wealthy move out of New York, New Jersey and other states to escape estate taxes.

Nor is it necessarily required to actually move anywhere for the affluent to avoid estate taxes.

In some cases, the highest earners aren’t going anywhere, just moving assets into trusts in states like Delaware and Alaska without estate taxes. William Lipkind, a New Jersey lawyer, told Bloomberg News he routinely moves clients’ assets out of state to avoid estate taxes, with the amount ranging from several hundred thousand dollars to hundreds of millions. “I can’t sit with a client who has a substantial portfolio or is contemplating selling his business without putting the strategy on the table,” Lipkind said. “You scratch your head and say, ‘Why pay if we don’t have to?’”⁶⁸

Connecticut’s high estate tax rate hasn’t translated to higher revenues. In 2009, estate and gift taxes made up 1.9 percent of total tax revenues, declining to 1.1 percent by 2019.⁶⁹ This may also be a sign that would-be taxpayers have found ways of avoiding them.

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No longer Taxachusetts

Defenders of Connecticut’s tax policies point to the fact that it has lost a considerable amount of wealth over the last few years to Massachusetts. Given the Commonwealth’s old Taxachusetts label, they claim this demonstrates that Connecticut’s tax policies are not a major factor in the exodus of wealthy taxpayers from the state.

But this argument is rooted in an outdated view of the Bay State’s tax and budget policies. Connecticut has hiked its income tax four times since 2003 compared to just once in the last 30 years for Massachusetts.

In the midst of a dire budget crisis during the 1990–1991 recession, Massachusetts lawmakers voted to hike the income tax to 6.25 percent and then drop it down again in 1992 to 5.95 percent.⁷⁰ Nearly a decade later, Massachusetts approved a ballot question to bring the income tax rate back down to 5 percent. State lawmakers later attached a series of conditions designed to make the decline in the income tax rate a gradual process, with a .05 percent drop each year in which certain revenue markers are met. By 2020, the rate had reached its target of 5.0 percent.⁷¹

State lawmakers roundly rejected a proposal by Gov. Deval Patrick in 2013 to hike the income tax rate back to 6.25 percent to spend more on transportation and infrastructure projects.⁷² While Massachusetts adopted a combined tax reporting system of the type GE protested so vehemently in Connecticut, it also knocked its corporate tax rate down from 9.5 percent to 8 percent.⁷³

From 1977 to 2012, Massachusetts saw one of the largest tax reductions in the country, with residents’ local and state tax burden dropping from 12.3 percent to 10.3 percent. Only Alaska and North and South Dakota saw bigger drops.⁷⁴ Once one of the worst performers, Massachusetts is now solidly in the middle ranks of the Tax Foundation’s Business Tax Climate Index.⁷⁵

The Bay State’s relative restraint on taxes and spending helped set the stage for a quarter century of strong growth following the state budget battles and crises of 1988–1991. Massachusetts has created more and better jobs than Connecticut and other states across the Northeast, and real per capita income more than tripled from 1980 to 2019.⁷⁶

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Overall, Massachusetts gained some 411,000 net jobs from 2008 to 2020 for an increase of 12.5 percent, according to Pioneer's research. The state has recovered all the jobs lost during the recession and then some, with over 3.7 million people working in Massachusetts in 2020, compared to 3.3 million in 2008.⁷⁷ Before the COVID-19 pandemic, the state unemployment rate hovered near 3 percent, a 20-year low and down from 8.8 percent at the height of the Great Recession.⁷⁸

The Bay State's lower taxes and more vibrant economy are attracting millionaires at nearly twice the rate of Connecticut. Massachusetts saw the number of millionaires increase by 84.5 percent from 2009 to 2019, making it and New Hampshire the only northeastern states in the top one-third of the list.⁷⁹ That's also well above Connecticut's 57.3 percent millionaire growth rate.

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Conclusion

Connecticut has turned repeatedly to its wealthiest taxpayers to cover spending increases and is now suffering the consequences. Connecticut's governor and top legislative leaders were equally optimistic before the state's last major tax hike in 2015, with a spokesman for Gov. Malloy calling it an "historic investment" financed by tapping the state's richest families and companies. At the time, Mark Bergman, a spokesman for the governor, said "We are asking our wealthiest and our corporate community to help pay for a transformational transportation and infrastructure system that will benefit Connecticut's economy for decades to come."⁸⁰

As it considered yet another tax hike in 2015, Connecticut's legislature and governor shrugged off warnings from major employers like GE and Aetna that they would consider moving out of state if potentially damaging provisions like a unitary tax reporting system were passed. Years of red flags and other signs that the Constitution State's wealthiest families were also unhappy with the state's tax policies also went unheeded.

However, the state's third tax increase in six years failed to usher in a new era of prosperity or even solve Connecticut's persistent budget woes. Instead, Connecticut's economic growth practically ground to a halt in 2016, with a drop in income tax revenue from the state's wealthiest taxpayers triggering another budget crisis in 2017.

This time, legislative leaders rejected plans to boost the state income tax for couples making more than \$1 million annually to 7.49 percent.⁸¹ Malloy, who just two years before had led the charge for higher taxes on corporations and the wealthy, talked lawmakers down from plans to impose a special tax on hedge funds, siding with Republicans who argued it would drive millionaires from the state.⁸²

While the Massachusetts economy has proven far more resilient and dynamic in recent years, there's no reason to think a similar scenario couldn't repeat itself here. Like Connecticut, the Commonwealth is reliant on a relatively small number of wealthy taxpayers, who foot a sizable chunk of the state's bills.⁸³

There are many reasons why wealthy families and corporations opt to leave one state for another, from weather to the business climate. While taxes are not the sole factor, they are nevertheless a consideration for companies and wealthy families alike, who routinely draw upon sophisticated advice from financial planners, accountants, and tax lawyers. Moreover, taxes are a factor that can become more important as rates escalate.

For those with the means to relocate, mobility has never been easier. The rise of instant communications and the ability to do business anywhere and anytime makes it fairly easy to change one's permanent address and effectively move income to a state with lower income taxes, or none at all.

Connecticut provides a sobering real-world example of how a seemingly attractive tax-the-rich scheme can backfire badly on a state, turning rosy projections of revenue gains to real-life losses, and damaging business confidence in the process.

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Pioneer Institute develops and communicates dynamic ideas that advance prosperity and a vibrant civic life in Massachusetts and beyond.

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Success for Pioneer is when the citizens of our state and nation prosper and our society thrives because we enjoy world-class options in education, healthcare, transportation and economic opportunity, and when our government is limited, accountable and transparent.

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