



MAXIMIZING THE IMPACT OF TAX CUTS

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Massachusetts' finances look very healthy, with tax revenues overflowing and aid from the federal government at unprecedented levels. State lawmakers are considering using some of this money for a package of targeted tax cuts.

Options abound, but with the legislative session set to end July 31, time is quite limited. This creates real risk, as poorly designed tax cuts could worsen inequality or generate future budget deficits.

To help lawmakers act swiftly and smartly, we have assembled this policy brief with the following core information:

- Key principles for avoiding risk and ensuring meaningful impact. This means balancing short- and long-term effects, looking at who benefits, and promoting economic competitiveness.
- Clear analysis of the options being discussed on and around Beacon Hill, including restructuring the estate tax, increasing child tax credits, and a great deal more. Wherever possible, we share cost estimates and offer concrete alternatives.
- Direct comparisons with other states, where there's broad interest in one-time rebates and the earned income tax credit.

PRINCIPLES FOR CUTTING TAXES

Tax cuts come in many varieties, with hugely differential effects. Some provide relief to the most vulnerable, while others disproportionately benefit the wealthy or create problems for the state's financial future.

When assessing options for a tax cut package in Massachusetts, it's important to focus on the following issues:

Short-term vs. long-term effects. Yes, state coffers are flush. But this may be a temporary windfall from emergency federal aid and Covid-related shifts in economic activity. In addition, there's real uncertainty about the state's long-term financial situation, hinging on whether voters approve a [millionaires tax](#) in November.

As a consequence, some of the tax cuts should probably be temporary. Otherwise, when today's good fortune dissolves, we may miss these lost tax dollars.

One potential solution is for lawmakers to add "sunset" provisions to any tax cuts, so they expire after three or four years. If effective and affordable, they can be renewed at that time.

Who benefits? With a clear goal and the right approach, tax cuts can be tailored to help virtually any group of residents: rich, poor, young, old, etc.

If lawmakers are interested in using tax deductions or credits to help low-income residents or promote racial equity, one key is refundability. This approach allows families to receive meaningful benefits even if they have limited earnings.

Improvements, not just cuts. Our tax code has a number of inefficiencies and anachronisms that can undermine long-term competitiveness. Now may be a good time to tackle these as part of a broader package.

One widespread example is the need for better inflation adjustments, so that the tax code keeps

up with our changing economy. Without these adjustments, deductions effectively shrink and tax credits get less valuable for families every year.

Time matters. The Legislature's need to act quickly sets a limit to what's politically possible because there isn't time for a full study of novel proposals or radical changes.

To minimize unintended consequences, it may be best to find "dials" within the existing tax code that can be easily adjusted, rather than wholly new strategies.

ASSESSING POTENTIAL TAX CHANGES

ONE-TIME REBATES

Perhaps the simplest approach to cutting taxes right now is to give all Massachusetts taxpayers a one-time rebate. This would be highly progressive and — because it's one-time — won't create any long-term burdens.

Ten other states are considering this approach for 2022, including an unusual mix of liberal and conservative names like Delaware, Colorado, Georgia, and New Mexico.

Costs would depend entirely on the size of the rebate. A \$100 rebate for individuals, and \$200 for married couples, would run roughly \$500 million. The Department of Revenue could distribute these rebates at any time.

CHILD AND DEPENDENT TAX CREDITS

One lesson from the federal government's pandemic response is that offering money to families with young kids pays big dividends in terms of [reducing child poverty](#).

And while the federal program has been curtailed, Massachusetts can expand its own efforts.

Governor Baker has proposed doubling the state's two refundable tax credits for young kids at a cost of around \$165 million in the first year. This change

is relatively easy to implement, and would have a strongly progressive impact.

A simplifying alternative is to consolidate these two tax breaks — one of which offers a more valuable credit to families who itemize their expenses while the other provides a less generous credit to those who don't.

With a consolidated credit, taxpayers wouldn't need to itemize or present receipts. Instead, all families with children under 13 or dependent adults would qualify for a refundable credit of \$400 to \$500 per child — perhaps up to three children instead of the current cap of two.

Depending on the size of the credit, consolidation would cost roughly [\\$100 to \\$150 million more per year](#) than the governor's proposed change.

ESTATE TAX

It is widely acknowledged that Massachusetts' estate tax is badly designed and out of step with other states. Not only does it apply to estates as small as \$1 million — tied for the lowest threshold in the nation — but it has a weird “cliff” setup where estates just over the \$1 million mark face an unusually high marginal tax rate.

Proposals to fix these problems generally entail large tax cuts for some of the richest households in the state. The Massachusetts Department of Revenue estimates that raising the cutoff to \$2 million and eliminating the cliff [would have cost about \\$230 million in 2017](#) — or almost half of all estate tax revenue. It also would have shaved \$84 million from the tax bills of the wealthiest 20 percent of estates.

One way to improve the tax without sacrificing quite so much revenue is to simultaneously adjust the rate table. To return to the 2017 example, if estate tax rates were increased by one-quarter, the Legislature could eliminate the cliff, double the cutoff to \$2 million, and still collect \$320 million.

Another approach is to adopt the thresholds and rate table of a state with a [better-designed estate](#)

[tax](#), such as Connecticut, Vermont, or Maryland. These states generate meaningful revenues with a tax that applies only to much larger estates (\$5 million for Vermont and Maryland, \$7.1 million for Connecticut.)

Note: The estate tax threshold should also be adjusted for inflation, so that it doesn't apply to ever-more estates over time.

EARNED INCOME TAX CREDIT (EITC)

With decades of proven results, the EITC may be the most widely supported tax credit for low-income families, providing a once-a-year payout to people with some work history.

Last year, [over a dozen states](#) chose to boost the generosity of their EITC programs, and Massachusetts could easily do the same.

Currently, we offer an EITC credit equal to 30 percent of the federal version. Raising the match to 50 percent would cost around \$175 million per year; doubling it would cost \$260 million. Such changes would be simple to implement.

Another option is to widen eligibility for EITC. Currently, the credit isn't available to workers under 25 or over 64 — and that top age limit is especially difficult to justify with Social Security eligibility rising to 67. Access to EITC could also be offered to noncitizen immigrants who file taxes with an ITIN (rather than a Social Security number) at an [estimated cost of \\$10 to \\$15 million annually](#), under current rules.

NO TAX STATUS

Currently, individuals earning less than \$8,000 are exempt from the Massachusetts income tax. Increasing this “No Tax Status” threshold to match the federal level, as the governor has proposed in his tax package, would help hundreds of thousands of lower-income residents.

This approach is extremely cost effective, as it involves relatively small amounts of relief — generally less than \$200 — targeted directly toward the very-low-income families who would benefit most.

However, this change may not be easy to implement as there are some technical problems to work through.

The “No Tax Status” provisions interact with other parts of the Massachusetts tax code. For instance, we also provide a Limited Income Credit for individuals earning between \$8,000 and \$14,000. Would this disappear if the no tax status jumps to \$12,400, as in the governor’s proposal? Or would it be shifted in tandem? Similar issues arise for the personal exemption, and they all need to be addressed in order to avoid kinks in the tax credit system — or places where people would be better off if they earned less money.

UNEMPLOYMENT BENEFITS

By definition, people collecting unemployment insurance have suffered a major loss of earnings. Wholly or partially exempting their unemployment benefits from taxes — just as the state did during the pandemic in 2020 and 2021 — might be a one-time tax cut for lawmakers to consider.

Not only is it a short-term change targeted to those in need, but it’s easy to implement and relatively inexpensive, given the strong job market. Recent experience should allow the Department of Labor and Workforce Development to provide a timely estimate of the cost.

RENT DEDUCTIONS

Renters are currently allowed to deduct a small portion of their rental costs from their taxes, up to \$3,000 per year. Increasing the deduction to \$5,000, as the governor has proposed, could provide valuable relief — particularly as the \$3,000 cap hasn’t been raised since 2001.

But the impact would be limited by the fact that this deduction is not refundable. And there’s reasonable concern that rents would rise as a result. These issues mean the rental deduction isn’t as well-targeted as other approaches.

Either way, the renter’s deduction should be indexed to inflation so as to keep up with rental costs over time.

SENIOR CIRCUIT BREAKER

Retirees sometimes struggle to pay property taxes because their homes are expensive but their incomes are limited. To help, Massachusetts has introduced a number of different programs, including a refundable tax credit generally referred to as the “senior circuit breaker.”

The governor’s proposal to double the size of this credit isn’t particularly expensive, and would definitely help some retirees.

But seniors are somewhat insulated from current economic challenges. Note, for instance, that the circuit breaker credit is already indexed for inflation, so it will rise automatically. And Social Security benefits are also inflation-adjusted, meaning that seniors’ income will largely keep up with price increases.

A better approach may be to [encourage participation in other programs](#) that help seniors cover their property tax bills — ideally by making these programs better known and easier to join.

BETTER TAX POLICY

Passing a package of tax cuts is an opportunity to improve our tax system. And there are a lot of important, relatively low-risk changes to be made.

- The rules governing our income tax system are grossly outdated and need to be [brought into conformity](#) with the federal government’s current internal revenue code.
- To help policymakers and researchers understand how our tax system is evolving, DOR should release more regular and more consistent data about tax payments. One straightforward requirement would be a state version of the IRS’s “statistics of income.” Piggybacking on the IRS approach would offer a proven framework for rapid implementation and release.
- Refundable tax credits provide an annual, lump-sum payment — whereas low-income families might benefit from more regular, monthly distributions. Shifting to a monthly schedule is

tricky, but the Legislature could appoint a technical committee to assess the viability of monthly child credit or EITC payments.

- Optimizing our corporate tax code will be an important challenge for the next legislative session, potentially including issues like switching to single sales factor apportionment and eliminating the non-income measure of the corporate excise tax. In preparation, it may be helpful for DOR to analyze the cost of such changes.

CONCLUSION

Our mission at the Center for State Policy Analysis is to provide information, evidence, and guidance to help lawmakers address live policy challenges in Massachusetts.

At the current moment, one of those challenges is assembling a tax cut package that benefits the most vulnerable, improves our state's competitiveness, and avoids unintended long-term consequences.

We hope this brief clarifies the key issues and helps lawmakers identify approaches best-suited to their goals.



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