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State Tax Exemptions In The Cross Hairs

By CHRISTOPHER KEATING, ckeating@courant.com

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HARTFORD — In flush economic times, the legislature could leave untouched the huge number of exemptions from the state's 6 percent sales tax: haircuts, prescription drugs, boat repairs, car washes, and food purchased at supermarkets, to name a few.

But with a looming budget deficit, projected at \$3.5 billion in the next fiscal year, "everything is on the table," Gov. Dannel P. Malloy has said repeatedly.

He and his advisers have been conducting a comprehensive analysis of the state's complicated and extensive system of tax exemptions and credits, which total more than \$5 billion annually. On Wednesday, Malloy said he had not made any final decisions on proposed taxes. But he also would not rule out changing any exemptions, with one exception — those for charitable organizations.

More than \$3 billion worth of exemptions are related to the sales tax.

Eliminating the 6 percent sales tax exemption on food alone would generate \$400 million annually for the state, said one outside expert, Richard Pomp, a University of Connecticut law school professor and expert on tax law.

The food exemption is designed to help the poor because, compared with the wealthy, they spend a larger percentage of their income on food.

But Pomp said in an interview that the exemption is "a pretty stupid, inefficient way" to help the poor because the across-the-board exemption also covers multimillionaires in Fairfield County when they buy steak and lobster at the local supermarket.

Pomp, a tenured professor with a six-figure income, said it makes little sense for him — and others who are far wealthier — to receive the benefit.

"I'm perfectly capable of paying a tax on food," Pomp said. "Why do I get the exemption?"

Pomp spoke earlier this week at the 10th annual state budget forum sponsored by the New Haven-based Connecticut Voices For Children. During the presentation, state Rep. Andrew

Fleischmann of West Hartford asked Pomp about the political consequences of trying to remove the highly popular exemption.

"Yes, you have to face the voters, and I don't," Pomp acknowledged.

But Pomp said after the forum that he has been teaching about tax law for decades, and that the \$3.5 billion deficit gives the state the opportunity to take a comprehensive view of all exemptions. When the state is in surplus and the good times are rolling, "there is no great pressure to look into it," Pomp said.

"It is an idea. The time has come to think about it," Pomp said. "If you go South and West, food becomes taxable."

On Wednesday, Malloy said he was "not there" yet on any final decisions on tax increases or changes in the tax exemptions.

"We're still working on the spending side," said Malloy, whose budget will be presented to the legislature Feb. 16.

Although food is among the most prominent exemptions, Connecticut has more than 100 sales-tax exemptions that have found their way into the tax code through the decades. There is no sales tax, for instance, on prescription drugs, X-rays, dental visits, oxygen, telephone equipment for the deaf and blind, diapers, car washes, tax-preparation services, haircuts, boat repairs, winter boat storage and cremation services.

"The yacht repairs [exemption] was to steal business from Rhode Island," Pomp said.

Malloy has already publicly questioned why consumers must pay sales tax on their car repairs but are exempted for their boat repairs. As part of the ongoing analysis, he is looking at how Connecticut stacks up against its competitors.

"When we look more closely at revenue and tax expenditures specifically, I can assure you that the first questions I ask is: What's New York doing? What's New Jersey doing? What's Massachusetts doing? What's Rhode Island doing?" Malloy said Wednesday. "I'm keenly aware of the necessity of maintaining a substantial tax advantage" against neighboring states.

He was asked about the exemptions regarding food and prescription drugs.

"With the exception of trying to argue the case of changing the law with respect to charitable contributions and charitable organizations, everything else is subject to examination," Malloy said.

Connecticut currently has an advantage over the surrounding states, with a sales tax of 6 percent. Both New Jersey and Rhode Island charge sales taxes of 7 percent, while Massachusetts is at 6.25 percent. New York has a hybrid system of state and local rates that can total more than 8.5 percent, depending on where an item is purchased.

Connecticut's sales tax was previously 8 percent, but in 1991 it was dropped to 6 percent as part of a compromise to create the state income tax.

A national analysis by the Washington, D.C.-based Institute on Taxation and Economic Policy for all 50 states showed that the poor in Connecticut paid the highest percentage of their income on sales taxes — which suggests that they are the biggest beneficiaries of the exemption.

The analysis shows that the lowest 20 percent in income — earning an average of \$12,700 annually — pay 6.3 percent of their income in sales and excise taxes. Those earning an average of \$34,500 per year pay 4.5 percent of their income in sales tax, while those in the top 1 percent — earning \$1.35 million or more per year — pay 0.7 percent of their income in sales taxes.

The same analysis showed that the rich paid the highest share of the state income tax of any income group and that the poor paid the lowest.

According to census figures, the average family of four spent \$5,279 in 2008 on food purchased for consumption at home and more than \$3,800 for food away from home. The highest amount is for families earning more than \$150,000, who spent an average of more than \$13,000 a year for food.

State Rep. Marie Kirkley-Bey, a deputy House Speaker who represents some poor constituents in her district in Hartford, said: "If there's an intention to charge sales tax on food, it should be exempt for people who get food stamps. It disproportionately hurts people who are poor. If they're going to implement it and make it fair, they should exempt people on food stamps."

Currently, items purchased with food stamps are exempt from the sales tax, and Kirkley-Bey wants to keep it that way.