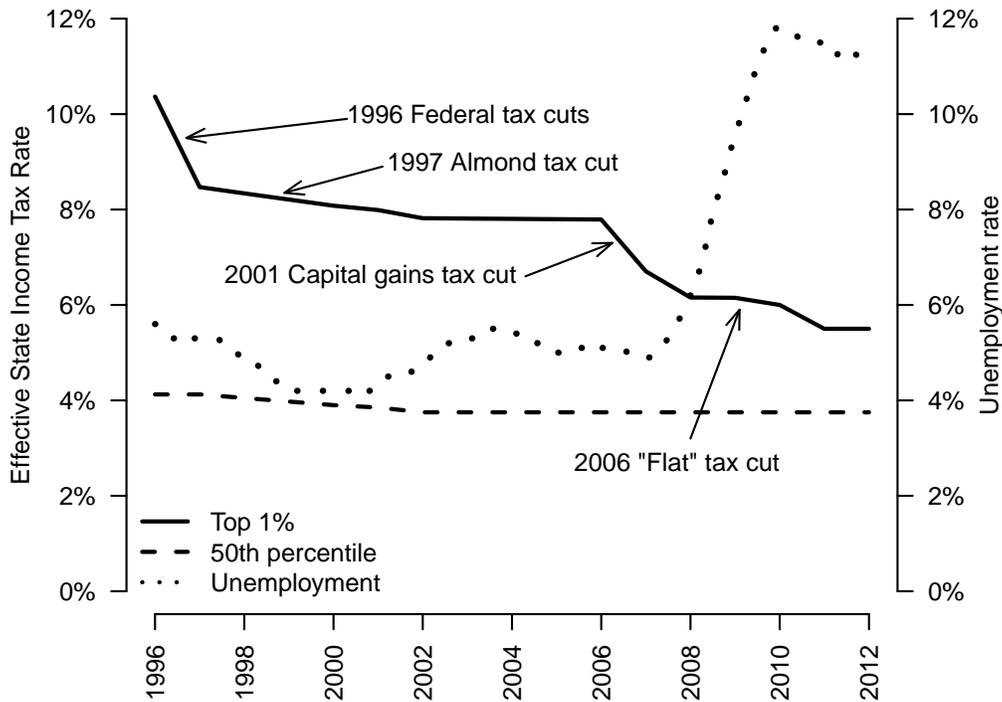


To: House Finance Committee  
 From: Tom Sgouros  
 Date: May 8, 2012  
 Re: Testimony in favor of H12-7454



In the graph above, the solid line is the effective RI income tax rate (total tax paid divided by total income) on a fairly typical taxpayer in the top 1% over the last 16 years, with the various cuts that taxpayer has received indicated. (Source: tax laws, RI and IRS statistics of income reports.) These cuts don't count tax credits like the film production or historic structures credits, which are typically only available to high-income individuals and which make the effective rate even lower. The dashed line indicates the effective tax rate on the median taxpayer (the 50th percentile). You can see a slight decline in the 1997-2002 period, but the other changes didn't do much of anything for them.

The dotted line indicates the unemployment rate, and is provided to show that there is little or no sign of any correlation between tax rate and unemployment rate. As the tax rate on the top brackets has been cut, there has been no more decline in unemployment rate than you would expect from any random event. From a statistical point of view, the two have nothing to do with each other.

Contrary to claims that our state's tax policy is brand new and needs time to work, this graph tells us the important aspects of income tax policy in effect today have been in

effect since 1996. Since that time, we have repeatedly lowered taxes on rich people and have yet to reap any measurable economic benefit at all.

## **How budgets are cut**

The real tragedy of the tax cutting of the past 16 years is that not a single one of the tax cuts passed by the General Assembly were paid for. The income tax cut of 1997, the car tax cut of the same year, the capital gains tax cut of 2001, and the flat tax cut of 2006 were all “phased in” to avoid having to make the tough decisions people are always talking about.

But the reduced state revenue had to be made up somehow, and I’d like to share with you my observations of the different ways to cut a budget:

1. Terminate a program or benefit.
2. Supply a program or benefit in a more efficient fashion.
3. Supply a program or benefit in a shoddier fashion.
4. Borrow to hide the shortfall.
5. Foist the cost onto somebody with another source of income.

In my review of state budget cuts over the past decade, I find very few examples of the first method. Certainly the Medicaid program is somewhat less generous than it was a decade ago. We cut services for *legal* immigrant children and pregnant women, for example. But how many other examples are there? I don’t support Governor Chafee’s proposal to terminate funding of WSBE television, but I applaud him for having the temerity to actually propose ending a fairly popular program.

For the second method, there are a few good examples. The recent reorganization at DMV might qualify. Though it also required some new personnel, they are now providing better service with not too many more people. DOT’s proposal to get designs and buildings from the same contractor has promise in this regard.

Unfortunately, too many of these border on examples of the third category. I believe this committee has, over the years, been insufficiently deferential to the judgment of department heads and experts about what is actually possible within the budget constraints presented. The transfer of 17-year-olds from the Training School to the ACI a few years ago is an example, and last year’s cut to BHDDH funding is another. The Department of Transportation’s shameful neglect of maintenance is yet another. Seventeen homes and four businesses in Tiverton are gone today because DOT didn’t maintain the Sakonnet Bridge adequately. Nor are they alone in their neglect of maintenance, as any visit to a state facility will attest. A few years ago, URI estimated the cost of deferred maintenance on their campus to be over \$400 million, not so much less than a year’s budget.

DOT has also been a prime offender in the borrowing category, but so have the colleges,

creating fancy new buildings while cutting back on the staff and projects that should be filling them.

It's the fifth category that has seen the most exercise. In the drive to cut taxes on rich people, the state has cut funding to: municipal governments and school departments who have to make it up with property taxes; to colleges who have to make it up with tuitions; to Medicaid recipients who have to make it up with co-pays; to everyone who fishes, drives, or runs a hospital who have to make it up with increased license fees, and to many more. These are the people who have paid for the tax cuts of the last 16 years.

Let's be clear: courage is not foisting costs off onto others, nor is it insisting the state do its job badly. It is not borrowing to hide shortfalls or pushing costs into the next year. Calling for efficiency is laudable, but it is not courage, either.<sup>1</sup>

Courage means honesty. It means assessing with honesty our past policies, and not hiding behind some claim that we have to wait and see what we've been waiting for over a decade to see. It means honestly assessing claims that rose petals will fall from the sky if only we can avoid asking rich people to pay their fair share. It means honestly assessing what our state needs to do and finding a fair way to raise all the revenue with which to do it. Honesty is hard, the reason it's equivalent to courage. Please be honest, please be courageous.

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<sup>1</sup>Nor should it be confused with actually *finding* efficiencies.