

State Tax Cuts After the Pandemic Strategies to Sustain Fiscal Health



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ISSUE
PAPER

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Analyze the implemented state tax relief measures in FY 2021 and FY 2022

- **39 states** made **92** substantial tax relief measures
- **A variety of forms and sizes:** permanent income tax rate cuts, one-time income tax rebates, temporary sales & gas tax holidays, expanded earned income tax credits
- Estimated cost: **\$124 billion** through 2028

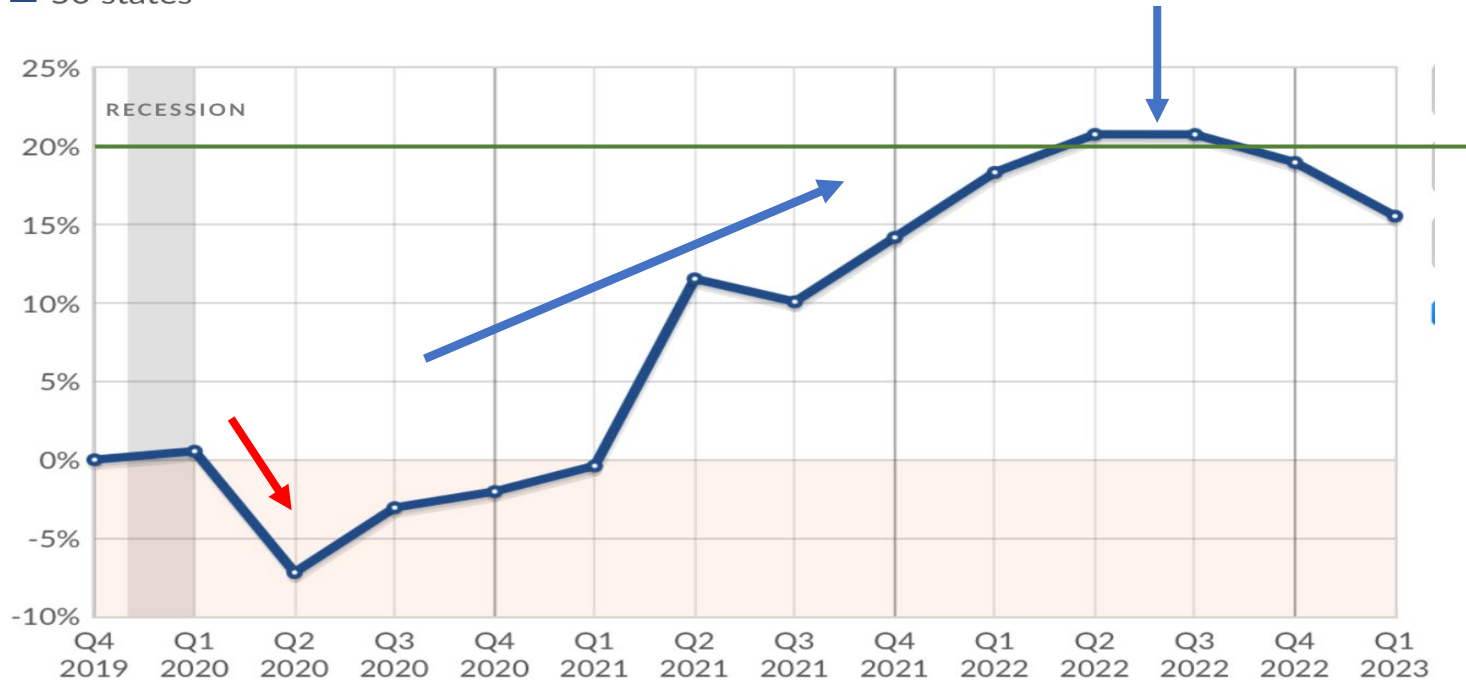
Discuss long-term fiscal impacts of tax relief measures

- **Permanent and costly tax cuts** on major tax sources pose long-term fiscal risks under uncertain economic conditions
- **Temporary tax cuts** (*tax rate reductions, rebates & holidays*) **targeted tax exemptions & credits** have modest effects on revenues and are more fiscally sustainable

Background: Tax revenues rebounded as economies recovered from the COVID-19 pandemic

Change in Tax Revenue From Each State's Pre-Pandemic Level

■ 50 states



Motivation

- **Unanticipated revenue surpluses** put states in a strong position to enact various tax relief measures due to robust tax revenue growth and a large amount of federal aid
- Governments often face long-term budget challenges when **they use one-time budget surpluses for permanent and expensive tax cuts**
- **Research questions:**
 - *How are state tax relief measures made after the pandemic?*
 - *What are the major types and estimated costs of state tax relief measures?*
 - *How are state tax relief measures paid for?*
 - *What actions would be needed to walk back state tax cuts (e.g., revenue triggers)?*
 - *What are the fiscal impacts of state tax cuts?*

Research Approach

- **Collected information on state tax policy changes:** state legislature bills, state budget summary documents, state audited financial statements, state recovery plans, and other related sources (e.g., Tax Foundation, CBPP, ITEP)
- **Selected five major tax cuts for in-depth case studies**

How States are Providing Tax Relief? Overview

TABLE I Tax Relief Measures, Fiscal Years 2021–22

TYPES OF SIGNIFICANT TAX RELIEF MEASURES	NUMBER OF STATES	TOTAL NUMBER OF SIGNIFICANT TAX RELIEF MEASURES
Personal income tax	33	54
Corporate income tax	12	12
Sales tax	11	11
Gas tax	8	8
Property tax	7	7

SOURCES State budget documents; authors' calculations.

State Individual Income Tax Relief Measures

TABLE 2 Personal Income Tax Relief Measures

TYPES OF RELIEF MEASURES	NUMBER OF STATES	STATES
Personal income tax rate cut	21	Arizona, Arkansas, Colorado, Georgia, Idaho, Indiana, Iowa, Kentucky, Louisiana, Mississippi, Missouri, Montana, Nebraska, New Hampshire, New York, North Carolina, Ohio, Oklahoma, South Carolina, Utah, Wisconsin
Personal income tax rebate	12	California, Colorado, Delaware, Georgia, Hawaii, Idaho, Illinois, Massachusetts, Maine, New Mexico, South Carolina, Virginia
Retirement income relief	10	Alabama, Connecticut, Georgia, Iowa, Maryland, Nebraska, New Mexico, Utah, Vermont, Virginia
Expansion or creation of earned income tax credits	5	Connecticut, Illinois, Maine, New York, Utah
Creation of child tax credits	3	Connecticut, New Mexico, Vermont
Increase in standard deductions	2	Georgia, Virginia

SOURCES State budget documents; authors' calculations.

- **Iowa** phased in a flat personal income tax rate of **3.9 percent** by 2026 from **0.33–8.53 percent** (cost exceed **\$1 billion annually**)
- In **South Carolina**, rebate plans were estimated to cost \$1 billion

State Corporate Income Tax Relief Measures

TABLE 3 Corporate Income Tax Relief Measures

TYPES OF RELIEF MEASURES	NUMBER OF STATES	STATES
Rate reduction	9	Arkansas, Florida, Idaho, Nebraska, Oklahoma, New Hampshire, Pennsylvania, Utah, Colorado
Top rate reduction and tax bracket consolidation	2	Louisiana, Iowa
Top rate reduction and tax phaseout	1	North Carolina

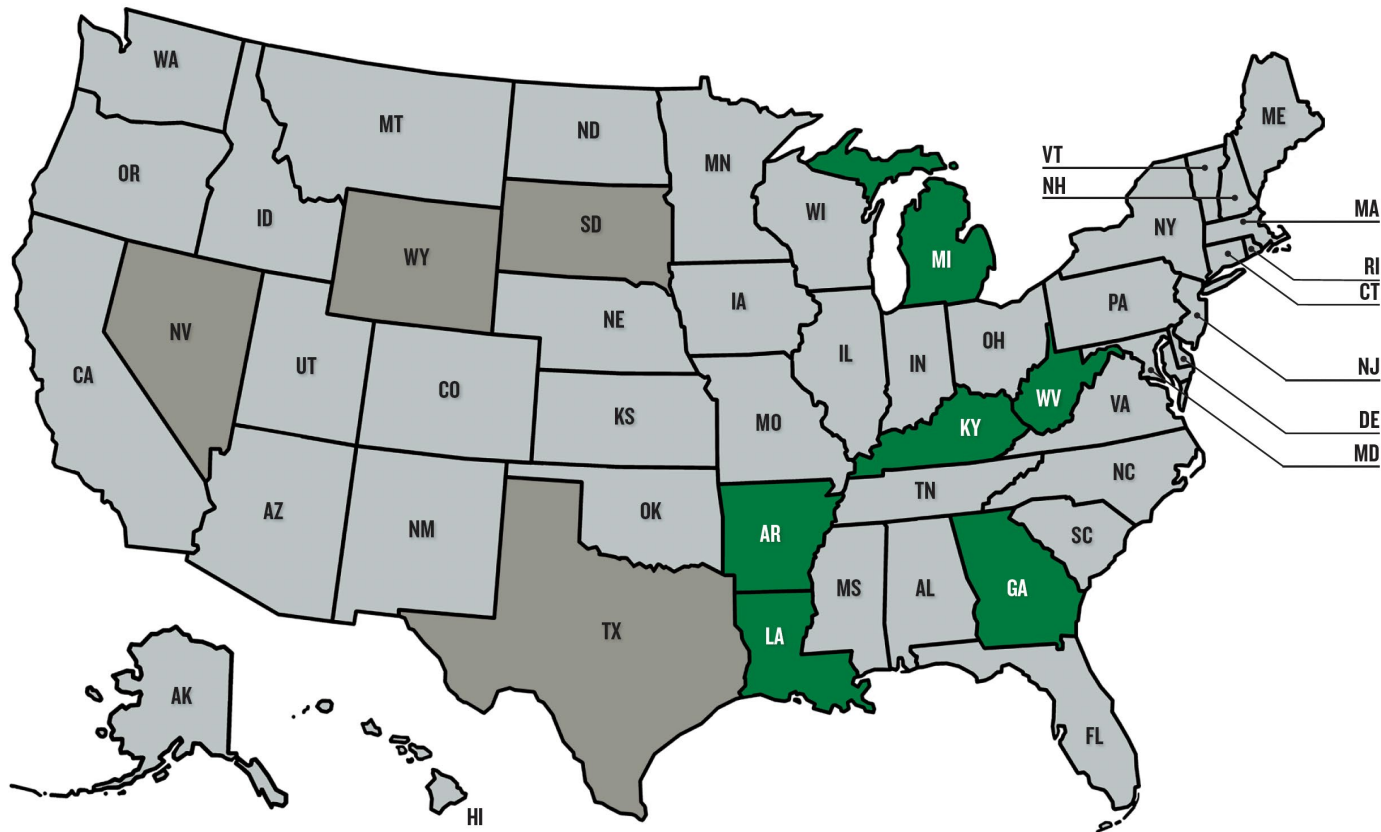
SOURCE State budget documents.

- In November 2021, **North Carolina** phased out the 2.5 percent corporate tax rate over five years, 2025–2030
- **Louisiana** consolidated a five-bracket corporate income tax system into three and cut the top rate 0.5 percentage point, to 7.5 percent for fiscal 2022

Tax Triggers

FIGURE 2 States with Active Income Tax Triggers, 2023

■ Personal cuts subject to trigger ■ States with no personal or corporate income tax



SOURCES State budget documents; authors' calculations.

State Sales Tax Relief Measures

TABLE 4 State Sales Tax Relief

TYPES OF SALES TAX RELIEF MEASURES	NUMBER OF STATES	STATE
New state sales tax holidays	5	Connecticut, Florida, New Mexico, New Jersey, Tennessee
State sales tax exemption on groceries	4	Kansas, Virginia, Illinois, Tennessee
State sales tax rate reduction	1	New Mexico
State grocery tax credit increase	1	Idaho

SOURCES State budget documents; authors' calculations.

- **Kansas** enacted a measure to phase out the 6.5 percent sales tax on groceries by fiscal 2025
- **Illinois** suspended its 1.0 percent sales tax on groceries for a year.

State Gas Tax Relief Measures

TABLE 5 Gas Tax Relief Measures

TYPES OF GAS TAX RELIEF MEASURES	NUMBER OF STATES	STATE
Gas tax holiday	5	Connecticut, Florida, Georgia, Maryland, New York
Delay of gas tax hike	3	Kentucky, Illinois, Indiana

SOURCES State budget documents; authors' calculations.

- **Georgia** began a tax holiday in March 2022 and extended it seven times to reduce the impact of inflation. The moves cost an estimated \$1 billion.

State Property Tax Relief Measures

TABLE 6 Property Tax Relief Measures

TYPES OF PROPERTY TAX RELIEF MEASURES	NUMBER OF STATES	STATE
Property tax rebate credit	4	Connecticut, Illinois, Nebraska, New York
Increase in state property tax exemption	2	Idaho, Texas
Reduction in property tax assessment rates and taxable valuations	1	Colorado

SOURCE State budget documents.

- **Illinois** increased rebates to \$300 for single filers earning up to \$250,000 and for joint filers earning up to \$500,000
- **Connecticut** raised its personal income tax credit for property taxes to \$300 from \$200

Discussion: Four strategies that state governments should consider when enacting tax reductions

Strategy One: Implement tax policy changes that are temporary and require reevaluation

Lower-Risk Strategies: Illinois, Delaware

Higher-Risk Strategies: Wisconsin

Discussion: Four strategies that state governments should consider when enacting tax reductions

Strategy Two: Incorporate well-designed trigger mechanisms to make prudent tax measure phase-ins.

Lower-Risk Strategies: Georgia

Higher-Risk Strategies: Iowa

Discussion: Four strategies that state governments should consider when enacting tax reductions

Strategy Three: Use refundable tax credits to provide targeted and more fiscally affordable tax relief measures for those who need it most.

Lower-Risk Strategies: Maine, Connecticut

Higher-Risk Strategies: Arizona

Discussion: Four strategies that state governments should consider when enacting tax reductions

Strategy Four: Use long-term forecasts to inform changes in tax policy

Long-Term Fiscal Planning Tools (Florida): Multiyear forecasts and legislative fiscal notes to identify medium- and long-term fiscal challenges

Budget Stress Tests (Utah): Anticipate and craft prudent fiscal responses to potential economic downturns.