ECONOMIC IMPACT
OF THE
PARTNERSHIP FOR GROWTH
TAX PROPOSALS

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The State of Connecticut has embraced the cluster concept as mechanism for promoting economic growth. *Partnership for Growth* is the first major publication produced by this cluster initiative. It contains a number of recommendations to make Connecticut businesses more competitive within an ever-expanding world market and bring economic growth and prosperity to Connecticut.

A series of tax proposals from the *Partnership for Growth* were recently presented to Connecticut State Legislature. Before adopting the proposals, the Legislature has asked the Department of Economic and Community Development to determine the economic and tax impact of each proposal. The work of studying the economic and tax impact of the proposals has been assigned by the Department of Economic and Community Development through its standing contract to the Connecticut Center for Economic Analysis at the University of Connecticut.

The professional staff of the Connecticut Center for Economic Analysis studied the impact of the tax proposals utilizing the econometric model of the State of Connecticut housed at the University of Connecticut. The model was built and calibrated by Regional Economic Models, Inc. of Amherst, Massachusetts. Regional Economic Models over the years has built econometric models of nearly every state in the United State and many counties within these states. Their models have become the standard for doing regional economic impact studies.

Proposals

Three of the tax proposals put forth from the *Partnership for Growth* are analyzed in this report. The first proposal, labeled “Section 1”, would extend the carry-forward period for net operating losses from 5 years to 20 years. OPM has estimated that this proposal would cost the State of Connecticut $50,000,000 per year.

“Section 2” extends the carry-forward period for the 20% incremental research and development tax credit to 20 years. It also allows the salability of the tax credits. OPM has estimated that this proposal would have a $20,000,000 per year price tag.

The removal of the graduated scale for tax credits for non-incremental research and development and its replacement with a flat 6% credit is “Section 3.” The proposal also contains the provision that these credits can be sold. With the salability provision included, OPM has estimated that this provision will cost $100,000,000 per year in tax revenue.

Economic Impact

All three proposals have been analyzed by the Connecticut Center for Economic Analysis. A summary of the Center’s finding is given in Table 1 below.

Table 1: Partnership for Growth Tax Proposals Economic Impact 1999-2008			
	Tax Proposal		
Economic Variable	Section 1	Section 2	Section 3
Gross State Product (Annual Average) Million 92$	$55.49	$106.79	$543.79
Total Employment (Annual Average)	598	1,146	5,842
Personal Income (Annual Average) Million $	$38.24	$74.11	$376.85
Disposable Income (Annual Average) Million $	$31.12	$60.22	$306.22
Population (Annual Average)	933	1,663	8,454
New State Revenue (Total) Million $	$23.77	$45.97	$233.69
New State Revenue (Present Value) Million $	$14.87	$28.76	$146.23
New Local Taxes (Total) Million $	$10.57	$20.23	$103.10
New Local Taxes (Present Value) Million $	$6.68	$12.81	$65.34

All three proposals bring economic growth to Connecticut. "Section 1" causes gross state product to increase by $55.49 million 1992 dollars on average per year. Sections "2" and "3" have even greater impacts. $106.79 million 1992 dollars of new gross product per year are the benefits of the adoption of "Section 2." The real winner in terms of new gross state product is "Section 3." It increase gross state product annually by $543.79 million 1992 dollars. For all three proposals, new gross state product grows with time. It takes a period of years for new research and development to be translated into more efficient production techniques and new and more competitive products for sale on the world market. The time paths for the gains in new gross product under the three proposals are given in Figure 1.

In addition to new gross state product, the three proposals will create new jobs. The annual average increases in new total employment are 598, 1,146 and 5,842 jobs for the three proposals respectively. The time paths for new jobs also increase over time. However, they do not grow as rapidly in the latter years as gross state product. This reflects the fact, that part of the new research and development encouraged by these proposals has gone to developing more efficient production techniques. These techniques permit the firms to expand their output without a corresponding increase in employment of new workers. The time path of new employment for the three proposals is shown in Figure 2.

At a more personal level, personal income grows as a result of adopting these three tax proposals. The annual average increases in personal income are $38.24 million, $74.11 million and $376.85 million for the "Sections '1', '2' and'3'" respectively. Figure 3 illustrates the time paths of the new personal income for the three proposals.

These proposals are designed to level the playing field for Connecticut firms in the world market. They will give Connecticut firms the same benefits they might obtain by relocating to other states. The growth of small innovative firms is one of the primary objectives of these proposals. These gains do not come without a cost. None of the proposals will generate sufficient new economic activity to return to the State of Connecticut new tax revenues sufficient to cover the direct tax cost of the proposals. Table 2 contains the estimates of the direct tax cost of each proposal, the new tax revenues generated and the implied tax cost of each new job to be created in Connecticut by these proposals.

Table 2: Economic Impact Partnership for Growth Tax Proposals
(Annual Averages 1999-2008)[1]

Section	OPM Tax Cost	New Tax Revenue	New Employment	Net Tax Cost per job per year
1	$50M	$2.4M	598	$79,600
2	$20M	$4.6M	1,146	$13,400
3	$100M	$23.4M	5,842	$13,100

The new State tax revenues for the three proposals have present values in 1998 of $14.87 million, $28.76 million and $146.23 million respectively. The time paths by which the State of Connecticut will reap these new taxes for the three proposals are shown in Figure 4.

[1] These estimates are the best case scenario. They assume sufficient surplus to absorb the tax cut without having to cut any existing State spending. More refined estimates can probably be developed when CCEA and OPM get an opportunity to discuss some other key elements of the existing tax codes and collections. Scenario 1 was run as if there was an equivalent cut in the corporate tax rate. Scenarios two and three were run using a corresponding tax credit variable, and hence induced meaningful investment activity.

Executive Summary

Summary

The *Partnership for Growth* tax proposals will increase Connecticut's future economic activity. They will generate new gross state product, new jobs, new personal income and new tax revenues. None of the proposals, however, will generate sufficient new tax revenues for the State of Connecticut to cover their direct tax costs. Connecticut legislators will have to decide the importance of a level playing field for Connecticut businesses in the future as they compete in an ever-increasing competitive world market. Are the new jobs created for Connecticut citizens by these proposals worth the price tags? This is the second question legislators will have to ask themselves as they vote on the proposals.

Figure 1: Partnership for Growth Additional Gross State Product 1999-2008

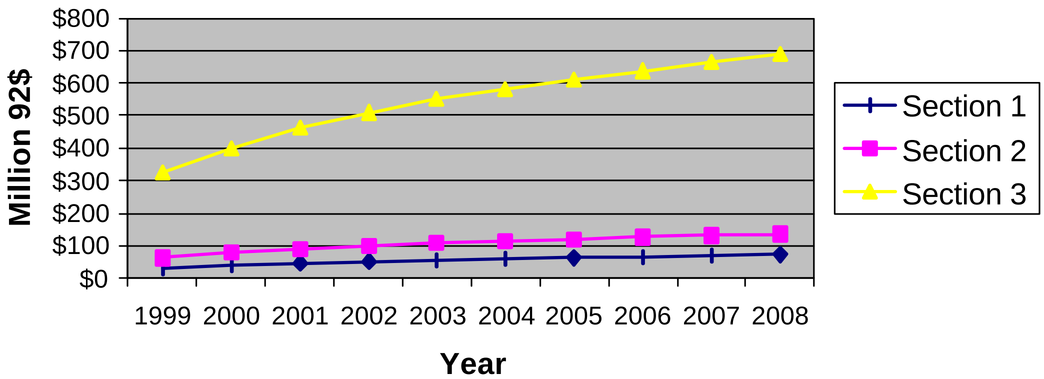
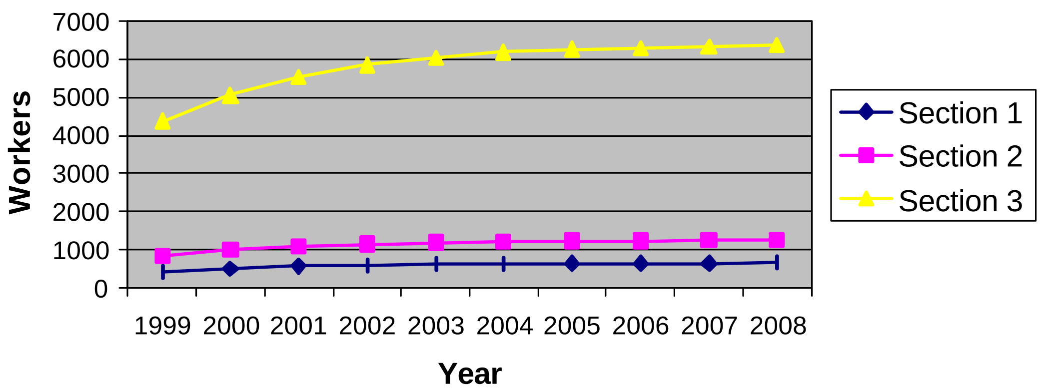


Figure 2: Partnership for Growth Additional Total Employment 1999-2008



CCEA
University of Connecticut

Figure 3: Partnership for Growth Additional Personal Income 1999-2008

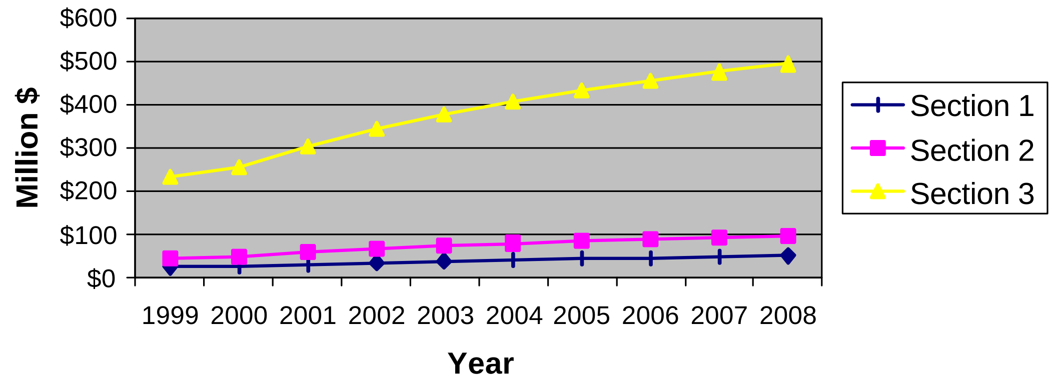


Figure 4: Partnership for Growth Additional State Revenue 1999-2008