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# Higher Taxes Wouldn't End Some Deficits

By MICHAEL POWELL

As state governments struggle with the fiscal damage caused by the recession, an income tax increase has become a rarely used remedy.

Governor after governor has publicly forsworn the prospect of raising income taxes, preferring to talk layoffs and cuts in programs and public union benefits. To cite prominent examples, Democrat [Andrew M. Cuomo](#) of New York and Republican [Chris Christie](#) of New Jersey have ruled out income tax increases.

Still, cracks have appeared in the no-tax-increase facade. In Illinois, Gov. [Pat Quinn](#) signed a law that temporarily raises the income tax rate to 5 percent, from 3 percent. New governors Mark Dayton of Minnesota and [Jerry Brown](#) of California have talked of enacting or extending tax increases.

Set aside for a moment the ever-charged argument about whether income tax increases spook the wealthy and consider this question: What would an increase in the personal income tax of a size similar to that of Illinois do for other fiscally troubled states? The New York Times examined this question in three embattled places, New York, California and New Jersey.

In New York, an increase of two percentage points in the state income tax could raise about \$9 billion and perhaps tip the state into surplus.

In California, a similar action could raise more than \$13 billion, which would cover just a portion of that state's yawning \$25 billion deficit.

In New Jersey, a jump of two percentage points in each of its income brackets could raise nearly \$5 billion, which would probably leave the state with a \$4 billion to \$7 billion deficit. Under these assumptions, a household with the median income would pay at least \$1,000 more a year in each of these states; a family making \$200,000 would pay \$4,000 more.

That an income tax increase of such a size could not close budget gaps in California and New Jersey underlines the vast challenge confronting these states. In California, Mr. Brown has proposed a deep, billion-dollar cut in higher education and \$4 billion worth of cuts in services for the poor and unemployed. Even a substantial increase in its state income tax — already much higher than in Illinois — would only soften the harshest blows.

In Illinois, too, the income tax increase will not cover all the accumulated ills, from a multibillion-dollar deficit to a backlog of unpaid bills to its huge pension problems.

For other states, though, such a tax increase would go much further in addressing at least the short-term problems. In Arizona, for instance, legislators during the last 17 years repeatedly cut income taxes, opening an annual hole of nearly \$2 billion. That sum, according to Mark Muro, a senior fellow at the [Brookings Institution](#), approximates the size of the state's annual deficit without taking into account the recession-driven drop in revenue.

Matthew N. Murray, a professor at the [University of Tennessee](#), Knoxville, who has studied state fiscal problems for the Brookings Institution, said: "In Illinois, the stark reality of the cataclysmic nature of their budget reality drove this income tax increase. But we're going to see more states raising taxes over the course of the next few years largely because there's only so much cutting you can do.

"It's getting to be a cold winter out there."

The Tax Foundation, no friend of tax increases, noted recently that many states face gaping revenue shortfalls and forecast that “2011 may be a year of dramatic tax increases.”

Many caveats attend this back-of-the-envelope exercise, not the least of which is that a comparison of California, New Jersey, New York and Illinois is inherently difficult. Illinois has a flat income tax rate (that is, residents regardless of income are taxed at the same 5 percent rate), while the other three have tax rates graduated by income, which is to say that a well-to-do couple pays taxes at a higher rate than does a working-class couple.

Illinois legislators, too, had the advantage of starting from a low base. The state’s 3 percent income tax rate was among the lowest in the nation. And the decision of the governor and legislature to raise taxes still leaves Illinois on par with — or slightly below — most neighboring states.

The new Republican governor of Wisconsin has lampooned Illinois for raising taxes, and he has invited its businesses and residents to move north. But Wisconsin’s income tax rate is higher over all than that of Illinois. Income tax rates in Wisconsin range from 4.6 percent to 7.75 percent, and someone earning \$10,000 or more gets taxed at least as much as a resident of Illinois.

Note also that Illinois cannot balance its budget with the personal tax increase alone; the state has also raised its corporate income tax and capped how much spending can grow.

Another caveat is that an increase of two percentage points in the rate brackets would leave California with the highest upper-income tax rate in the nation. And New York and New Jersey would not be far behind.

The talk of such income tax increases, it should be emphasized again, is a thought exercise. It arises from an intriguing fact, however, that tends to set this recent recession apart from earlier downturns. In the recessions of 2001, 1990-91 and most forcefully after the deep dive of 1980-82, state and local governments cut deeply and made layoffs. Then a number of states and cities enacted income tax increases to repair the damage as the economy slowly turned upward.

Not so in this recession.

“In a typical recession, you’d look for tax increases this year, as states already have cut a lot,” said Donald J. Boyd, a senior fellow at the [Nelson A. Rockefeller Institute of Government at the State University of New York](#) in Albany. “But we’re in quite an extraordinary antipublic union, antitax climate right now.”

A number of states, in fact, including Maryland, New Jersey and North Carolina, let taxes on high-income residents expire this year.

Oregon was one of the few to buck that trend. Last January, voters approved a temporary increase in taxes for individuals making more than \$125,000 a year and on couples whose income exceeded \$250,000. An editorial in *The Wall Street Journal* later stated that these rates caused thousands of upper-income residents to flee the state, but studies revealed that a large majority simply made less money, and so fell beneath the income cutoff for the higher rates.

What’s clear is that almost everywhere the fiscal crisis of states has grown more acute. Rainy day funds are drained, cities and towns have laid off more than 200,000 people, and Arizona even has leased out its state office building. Tax revenue has rebounded a touch as the economy recovers, but for now that is more than offset by the expiration of federal stimulus aid.

So the forecast grows darker.

“It’s the time of the once unthinkable, although it’s difficult to imagine other states following in Illinois’s footsteps with such a large increase,” noted Lori Grange, deputy director of the Pew Center on the States. “Whether there are tax increases or dramatic cuts to education and vital services, the crisis is bad, and there’s a bit of denial about how much government can provide and what it takes.”

*Amy Schoenfeld contributed reporting.*



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