STATES CAN HELP FUEL AN ECONOMIC RECOVERY FOR ALL BY TAXING WEALTH AND HIGH INCOMES

Families' access to wealth has played a large role in determining how the COVID-19 pandemic has affected them. The worst of the economic and health effects have largely bypassed wealthier, higher-paid families—which are disproportionately white—but have been far more prevalent among lower-income families and those of color.

Amid sizeable state revenue shortfalls and an unequal recovery that has exacerbated racial inequities, states would be well-advised to raise taxes on wealthy families to preserve funding for crucial priorities that can promote an equitable recovery—among them education, increased health spending to contain the pandemic, and boosts to cash assistance and other programs to help struggling families make ends meet during the crisis.

Other approaches states could take to balance their operating budgets—as nearly all states must do each year—risk worsening racial inequities, increasing hardship, and slowing the economic recovery. When states cut funding for schools, health care, or other services, it typically results in layoffs, which reduce economic activity and can deepen and prolong a recession.

Tax increases that ask more of low-income households as a share of their income would have a similar effect: many of these households are already spending far less due to job losses and the recession, and this would only reduce their consumption further. Wealthy households, meanwhile, are far less likely to respond to tax increases by reducing their consumption significantly.

Tax increases at the top are also better for state economies during a recession than spending cuts. Progressive tax increases allow for much-needed public investments that keep money flowing through states' economies by staving off layoffs and enabling states to maintain spending. Unlike individuals with low incomes, wealthy and high-income individuals generally maintain their spending levels regardless of a tax increase.

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States would therefore do well to address the preferential tax treatment available to affluent, high-income households, including steps to strengthen taxes on the following:

- **High wage and salary income.** Most states now have upside-down tax systems in which those who earn the least pay the most as a share of their income. Opting instead to raise personal income tax rates on the highest-income households, such as through a "millionaires' tax" (i.e., a tax on people with annual incomes exceeding $1 million), is a sound way to tax high income and help form a more solid foundation for a state's tax base.

- **Real estate.** "Mansion taxes" on high-value homes, or on their sale or purchase, are an attractive option for states looking to tax wealth, especially with the economic crisis having largely spared the high-value housing market.

- **Income from capital gains,** the income that an investor receives when a financial asset is sold for profit, is highly concentrated among the wealthiest households. The stock market's strong performance despite the pandemic is boosting those profits for many wealthy families. Options to raise taxes on this income include eliminating tax breaks on it and raising the rates it is subject to, either permanently or as a pandemic surcharge.

- **Inherited wealth.** We recommend that states that have no estate or inheritance taxes on wealthy individuals implement them, and states that already have such taxes should consider raising their tax rates or lowering the threshold at which the tax begins to apply. Current state thresholds range as high as $5.6 million, which can leave untaxed all but the wealthiest estates and thereby worsen inequality.

By improving the ways states tax wealth, lawmakers can help create a recovery and economy that works for everyone. This is essential not only for our COVID-19 recovery, but to build a state where our children and grandchildren can thrive, regardless of race or income.

About us:

The State Priorities Partnership shapes state policies that reduce poverty, advance equity, and promote inclusive economies that pave the way for widespread prosperity. It is coordinated by the Center on Budget and Policy Priorities.

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