The Effect of the President's Growth Package on State and Local Finances
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On balance, the President's Jobs and Growth Proposals will likely improve state and local government finances. The program promotes growth and creates jobs, boosting state and government revenues and more than offsetting the negative effects of the package on state and local finances.

The President's plan promotes economic growth and job creation.

- CEA estimates that if the package were enacted before July, it would increase the GDP growth rate by 1.0 percentage point in 2003 and by 0.8 percentage point in 2004. (Growth rates are fourth quarter to fourth quarter.) At the end of 2004, nominal GDP will be 2 percent higher with the package than without.

- The plan would create 510,000 jobs in 2003 and 891,000 jobs in 2004 – an increase of more than 1.4 million jobs in just 18 months. Private-sector economists reach similar or better results.

- The plan works well because it focuses on what the economy needs – more investment and support for continued consumption growth. The plan would reduce the cost of capital by more than 10 percent for new equity financed corporate investments. The lower costs stimulate investment.

- The plan provides $3.6 billion to states for re-employment accounts, which will help put people back to work and directly ease the burden on state finances.

The resulting economic growth will raise state and local revenue and more than offset any direct revenue losses to state and local government from the tax changes.

- Both simple and complex analyses of the effect of the package on all states and localities finances suggest a substantial positive revenue effect.

  - Assuming that state and local receipts (excluding grants in aid) simply increase along with GDP by their average share since 1980 would mean that state and local coffers swell by about $4 billion in 2003 and $18 billion in 2004, *before adding in any re-employment account funds.*

  - Using the *Macroeconomic Advisers (MA)* model to simulate the effects of the package, CEA has estimated that revenue would increase by $6 billion in 2003 and $19 billion in 2004, including re-employment account funds.

  - Both the simple share and CEA model-based estimates are similar to *MA's* own estimates, which point to increases of $5 billion in 2003 and $18 billion in 2004, also including re-employment account funds.

The projected receipts gains to state and local governments from higher growth are larger than the direct revenue losses.

- If states take no action to decouple from the federal income tax, the 100 percent dividend exclusion will reduce state revenues by about $3.3 billion in 2003 and 3.6 billion in 2004. (See table on last page for state-by-state estimates in 2003.) The expensing provision included in the President's package to encourage small businesses to invest will reduce state revenues by about $300 million in 2003 and 2004.

- The President's growth package won't directly affect other sources of state revenue. Local individual income taxes could be directly reduced somewhat, but the effect is likely to be small.

- On balance then, by increasing employment and income, the President's growth package can therefore be expected to increase aggregate state revenue by $1 to $2 billion in 2003 and $14 to $15 billion in 2004, even if no state decouples its tax treatment from the federal treatment.

States can easily adjust their tax systems to uncouple from the Federal dividend exclusion.

- Individual 1099 forms can potentially be used to report the total amount of dividend income received on state income tax forms.

- States could then require individuals to add back excludable dividends to adjusted gross income as reported on the Federal 1040 tax form.

- Adjustment to the increase in small business expensing could be handled similarly.

- Many states decoupled from Federal tax depreciation in response to the three year expensing provision included in the stimulus legislation enacted in March 2002.

Individual states and localities will benefit somewhat differently to the rising economic activity.

- Aggregate analyses suggest states and localities as a whole will benefit from the President's package. Research into the relationship between state individual income and sales tax revenue and general economic growth can help highlight potential differences among states. These two sources of revenue account for about 30 percent of all state and local revenues and over 50 percent of state revenues.

- On average, each 1 percentage point increase in national GDP boosts state individual income and sales tax revenue by about 1.2 percent. Table 1 shows how each state's revenue from these sources responds to changes in national GDP.

- The table shows that most states are likely to see greater-than-proportional gains in income tax and sales tax receipts as the economy responds to the jobs and growth package.

Table 1: Estimated State Sales and Income Tax Revenue Growth Resulting from 1 Percent Rise in GDP

0.9-1.0%	1.0-1.1%	1.1-1.2%	Over 1.2%
Wyoming	Oregon	Tennessee	Louisiana
Indiana	Oklahoma	Mississippi	Maine
Georgia	Kentucky	Missouri	Nebraska
Hawaii	Alabama	Colorado	North Dakota
Michigan	Utah	South Carolina	Connecticut
South Dakota	Texas	Arizona	Ohio
Illinois	West Virginia	Arkansas	Montana
	Virginia	Iowa	Nevada
	Delaware	Kansas	New Jersey
	Minnesota	Washington	New Mexico
	North Carolina	District of Columbia	Vermont
		Wisconsin	Rhode Island
		Idaho	California
		Maryland	
		Florida	
		New York	
		Pennsylvania	
		Massachusetts	

Note: Estimates use revenue elasticities reported by Richard Dye and Therese McGuire, 1998, "Block grants and the sensitivity of state revenues to recession," 1997 Proceedings of the National Tax Association, Washington, DC.

Table 2: Effect of Abolishing Double Tax of Dividends on State Tax Revenues, 2003

State	Excludable Dividend Income in 2003 1/	Starting Point for State Base 2/	Effective State Income Tax Rate 3/	Revenue Cost of Dividend Exclusion in 2003
		$ in millions		
Alabama	669	--	2.9%	20
Alaska	0	no income tax	0.0%	0
Arizona	1,246	FAGI	4.1%	52
Arkansas	535	--	6.6%	36
California	12,060	FAGI	7.0%	845
Colorado	1,288	FTI	4.1%	52
Connecticut	1,638	FAGI	4.3%	71
Delaware	312	FAGI	5.4%	17
District of Columbia	270	FAGI	8.4%	23
Florida	0	no income tax	0.0%	0
Georgia	1,688	FAGI	5.6%	95
Hawaii	288	FAGI	7.1%	20
Idaho	238	FAGI	6.5%	15
Illinois	3,675	FAGI	2.8%	104
Indiana	1,104	FAGI	3.2%	35
Iowa	568	--	4.5%	25
Kansas	619	FAGI	5.1%	32
Kentucky	657	FAGI	5.2%	34
Louisiana	643	FAGI	3.3%	21
Maine	307	FAGI	7.0%	22
Maryland	1,557	FAGI	4.2%	66
Massachusetts	2,468	--	5.0%	124
Michigan	2,413	FAGI	3.9%	95
Minnesota	1,228	FTI	6.6%	81
Mississippi	304	--	4.7%	14
Missouri	1,251	FAGI	4.7%	59
Montana	198	FAGI	7.4%	15
Nebraska	360	FAGI	5.6%	20
Nevada	0	no income tax	0.0%	0
New Hampshire	424	interest & dividends only	5.0%	21
New Jersey	3,071	--	4.4%	135
New Mexico	248	FAGI	4.4%	11
New York	6,350	FAGI	6.2%	393
North Carolina	1,650	FTI	5.7%	94
North Dakota	98	FTI	3.9%	4
Ohio	2,658	FAGI	6.1%	163
Oklahoma	466	FAGI	6.0%	28
Oregon	845	FAGI	7.4%	62
Pennsylvania	3,675	--	2.6%	97
Rhode Island	254	FAGI	5.7%	14
South Carolina	717	FTI	5.6%	40
South Dakota	0	no income tax	0.0%	0
Tennessee	943	interest & dividends only	5.6%	52
Texas	0	no income tax	0.0%	0
Utah	335	FAGI	4.8%	16
Vermont	202	FTI	5.7%	12
Virginia	1,938	FAGI	5.2%	101
Washington	0	no income tax	0.0%	0
West Virginia	242	FAGI	5.1%	12
Wisconsin	1,287	FAGI	5.6%	72
Wyoming	0	no income tax	0.0%	0
Total	**62,985**		**5.3%**	**3,321**

1/ Estimates based on dividend income reported on federal tax returns in 2000 adjusted to account for dividends that would not be excludable under the President's proposal and for growth in dividend income between 2000 and 2003. Only company stock dividends from corporate income fully subject to the corporate income tax would be excludable to shareholders.

2/ AGI=Federal adjusted gross income, TI=taxable income, -- does not use federal AGI as a starting point.

3/ Estimates take into account the distribution of dividend income and the progressivity of each state income tax.