Testimony to

SENATE SELECT COMMITTEE ON BUDGET AND TAX REFORM

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Senator Krueger and Committee Members:

Thank you for the opportunity to speak to you about taxation and economic growth in New York State on behalf of the 2,200 regional employers that Rochester Business Alliance represents.

Like you, we are proud to live and work in the Empire State. We are proud that most of the state's residents enjoy a high quality of life and excellent public services. And we are proud of our tradition of caring generously for the needs of the state's disadvantaged.

We can all agree that if we are to continue to support high quality public services, we need a healthy and vibrant economy. New York's economy must mobilize the skill and ability of the state's superb workforce and harness the entrepreneurial zeal of the state's business leaders.

We also can agree, as stated in the announcement distributed for this hearing, that New York's economy has been lagging—and not just in the current recession—particularly when compared to the growth experienced in many other states.

Yet your announcement suggests that our poor economic performance is at least in part a result of ineffective tax incentives. That's a conclusion with which we respectfully disagree.

The error, in our view, is to view the Corporate Franchise Tax in a vacuum. Admittedly, the corporate tax *RATE* is moderate by the standards of the nation. New York ranks 22nd in the country, according to an analysis by The Tax Foundation.

However, New York depends heavily on corporate tax revenues. In 2006, over seven percent of the state's tax revenue came from corporations, the sixth highest in the nation. On a per capita basis, New York is second highest in the nation. The collapse of the Wall Street finance sector may change this ranking, of course, which reinforces the need for policies that support economic growth.

What distinguishes New York from other states is the scope of its tax appetite. New York taxes pretty much everything. When all taxes are included, New York's overall tax burden is the second highest in the nation, barely behind New Jersey.

Of particular concern is the property tax. When viewed as a share of median home value, New York counties swept the top ten places and captured an astonishing 22 of the top 25 (in 2007). Monroe County had the unfortunate honor of placing fifth on this list with neighboring Orleans County taking the top spot.

Upstate has traditionally relied heavily on manufacturing. The industry's large investments in plant and equipment confer a similarly-large property tax burden.

The personal income tax (PIT) is also a major competitiveness factor. New York was second in the nation in tax collections per capita in 2007. The PIT affects business in two ways: First, many small businesses pay their taxes through the PIT, so increases in PIT rates means fewer dollars are available to invest in equipment, supplies and people. In a state dependent on the growth and success of small employers to help end the recession, an increase in the PIT rate harms small employers and the people that work for them.

Second, the PIT influences business location. A decision to expand an existing site, start a new venture or select a new location is made by individuals, not some impersonal "corporation." The decision-makers care about their own tax liability and that of their fellow employees. Concerned about high personal income and property taxes, individuals may choose a location that isn't as good for the business but is better for the employees. With the recent tax increases raising rates to 7.85% for married taxpayers earning over $300,000 and nearly 9% for filers with $500,000 or more in income, the personal income tax will be even more of a deterrent to decision-makers who believe that it may apply to them.

Direct taxes aren't the only competitive problem confronting business. For decades, the Legislature used the state's regulated utilities as proxy tax collectors. New taxes became built in the rate base and passed along to ratepayers, much as they passed along the cost of fuel. Legislators did it again in the 2009-10 budget, adding $600 million to the state's utility bills, in a state with electric rates that already lead the nation.

And this ploy has also been extended to the state's health care sector. The recently enacted budget added about $640 million to taxes through fees imposed on the health care providers and insurers. These increases will result in a cost-shift to employers and individuals, many of whom will be forced to drop coverage all together. The consequence of these significant new health insurance taxes will be an increase in the number of uninsured, placing an additional cost burden on the state and its taxpayers to provide health care for these individuals.

Taxes aren't the only cost of doing business in New York State. Businesses here are subjected to some of the most onerous regulations in the nation. And more are waiting in the wings. Senate Bill 1241/Assembly Bill 3659 (the Thompson/Hoyt IDA legislation) would impose the prevailing wage on all firms receiving assistance from industrial development agencies. Estimates by the nonpartisan Center for Governmental Research estimated that this would increase construction costs by an average of 28%. The cost of doing business is already too high.

In summary, New York's economic stagnation isn't the result of ineffective tax breaks, but an economic climate that discourages businesses from locating and expanding in this state. This anticompetitive economic climate is created by a comprehensive network of direct taxes, indirect taxes—through state charges and fees that drive up the cost of electricity, health care and other goods and services—and a daunting and confusing set of costly regulations.

You imply that we should eliminate some Corporate Franchise Tax preferences. **Let us instead simply eliminate the tax.** New York receives just over 7% of its revenue from the Corporate Franchise Tax. Eliminating the tax would spur economic growth, creating more revenue from every other tax, likely adding more to the state's coffers within only a few years of passage. At a minimum, the state should consider further Corporate Franchise Tax reductions, specifically for small businesses, manufacturers and other Upstate businesses.

Our problem isn't fundamentally about taxes. Taxes simply reflect a deeply entrenched habit of overspending. That New York State would choose, in these difficult times, to increase spending is staggering, particularly as the "golden goose" that made our decade-long spending spree possible is on life support.

Let us act boldly to cut spending. We urge New York State to:

- Empower local governments to take control of rising labor costs by granting more local control over the cost of public employee pay and benefits. This would include reforms like strengthening the "ability to pay" consideration in binding arbitration cases, and allowing municipal officials to participate in disability retirement proceedings.

- Empower local governments—including school districts—to renegotiate unaffordable contract provisions by repealing the Triborough Amendment to the Taylor Law.

- Cut onerous regulations and mandates that drive up cost, beginning with a complete review of administrative policies governing special education, which is responsible for huge increases in public school cost increases over the past twenty years.

- Reform Wicks Law threshold levels to reflect current economic realities. Wicks Law drives up construction costs by as much as 20 to 30 percent, causing local governments, school districts, and of course, taxpayers to pay more than they should have to for new buildings. The three-tiered threshold established last year that sets a $3 million exemption for New York City, $1.5 million for the surrounding suburbs and $500,000 for Upstate does not recognize the simple fact that Upstate needs more help, not less, as we try to turn our economy around.

- Create a Temporary Medicaid Reform Commission to review the Medicaid system and identify reforms to contain escalating costs. Combined federal, state and county Medicaid spending is expected to total over $46 billion in 2009-10. Considering the magnitude of this expense, it is imperative to find ways to deliver essential Medicaid services at an affordable cost.

- Approve a new Tier V in the state retirement system that will save money for local government and cut property taxes. The NYS Department of Budget has estimated that the state would save more than $48 billion over the next 30 years with this one reform.

We agree that tax reform is timely. For example:

- The Empire Zone program was originally structured to target economic development in distressed neighborhoods. While we continue to support this intent, we also believe that program benefits should be allocated by merit and not conferred “as of right” based on location. Zones might be assigned a flexible share of a fixed pool of benefits rather than an unlimited pool of funds for firms meeting the criteria.

- Tax expenditures should be targeted and tied to performance. While some flexibility is essential, especially during these difficult economic times, “clawbacks” should be enforced.

New York has a chance to come out of the current national economic crisis stronger than we entered it. But it won’t happen if we continue to do business as usual. We simply can’t afford to continue spending the way we do at local and state levels. We need political leaders to be willing to look beyond ideology and special interests and take a hard, practical-minded look at our problems and what we can do to solve them.

Thank you for the opportunity to speak to you today.