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Testimony on Taxes
Presented to the Joint Fiscal Committees of the NYS Legislature

Submitted by:

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NEW YORKERS FOR FISCAL FAIRNESS

New Yorkers for Fiscal Fairness

My name is Ron Deutsch and I am the Executive Director of New Yorkers for Fiscal Fairness. I would like to thank the distinguished members of the fiscal committees for the opportunity to provide testimony today.

My testimony will focus on the need to close corporate tax loopholes, reform some of our current corporate tax laws and the need to enforce our existing tax laws. I will also discuss the need to include property taxes under the purvue of the Tax Reform and Fairness Commission.

A Blueprint for Corporate Tax Fairness

New York could raise needed revenue and restore fairness to the tax code by reforming our state corporate tax structure and closing a variety of corporate tax loopholes to make sure small business and big business play by the same rules, and that higher profits are taxed at reasonably higher rates.

Last year's effort to make the PIT more progressive and more fair should continue in 2012 by reforming corporate taxes to close loopholes, end costly and ineffective tax subsidies, fix shortcomings that unnecessarily reduce tax collections and limit resources needed to maintain and invest in the infrastructure, services and educated workforce that foster long-term economic growth.

- REFORM PRINCIPLES: ENFORCEMENT, FAIRNESS AND TRANSPARENCY
- TARGETS: CORPORATE TAX EVADERS, REAL ESTATE PARTNERSHIP ABUSES, HEDGE FUNDS INCOME TREATMENT
- METHODS: TOUGH AUDITS, REASONABLE MINIMUM TAX FOR BIG BUSINESS, ELIMINATE HEDGE FUND SUBSIDIES, MANDATORY TAX REPORTING FOR PUBLIC COMPANIES

A simple, targeted corporate tax reform effort would provide over $1 billion in revenue for this year's state budget, and provide a start for the Tax Reform and Fairness Commission to continue reforms.

Tax Reform and Fairness Commission

In a press release that was issued by the three leaders after the December tax law changes were enacted it was announced that they had agreed to the creation of a Tax Reform and Fairness Commission. The release stated that, "The Governor is also establishing a commission to examine a comprehensive overhaul of the state's entire tax code that will make it simpler and fairer for all taxpayers and to create economic growth in the state."

In a later section of that press release, which provides additional detail on the agreed-upon "Fair Tax Code Reform," it is noted that "Through an executive order, the Governor **has created** the New York State Tax Reform and Fairness Commission to address long term changes to the tax system and create economic growth. The commission will have thirteen members, including four recommended by the Senate and Assembly majority leaders and two recommended by the Senate and Assembly minority leaders. The Chair of the Commission will be appointed by the Governor. All members are required to have expertise in the tax field and will receive no compensation. The Commission will conduct a comprehensive and objective review of the State's taxation policy, including corporate, sales and personal income taxation and **make revenue-neutral policy recommendations** to improve the current tax system. In its review, the Commission will consider ways to eliminate tax loopholes, promote administration efficiency and enhance tax collection and enforcement."

In the press release on the State of the State message http://www.governor.ny.gov/press/sos2012 , the Governor's Office, in relation to the **Establish(ment of) a Tax Reform and Fairness**

Commission, said that "Continuing efforts that began at the end of 2011 to reform the state tax code to boost job creation and improve fairness, Governor Cuomo announced the creation of the Tax Reform and Fairness Commission to propose additional, long-term changes to corporate, sales, and personal income tax systems, and to find ways to close tax loopholes, promote efficiency in administration, improve New York's business climate, and enhance collection as well as enforcement."

In the published version of the State of the State message the Governor, in relation to the **Establish(ment of) a Tax Reform and Fairness Commission**, said, "Our recent reforms to the state's tax code will boost job creation and restore fairness to the tax system. While these reforms were huge steps forward, there is more work to be done to create a complete fair tax plan. That is why I am creating a Tax Reform and Fairness Commission to propose additional, long-term changes to our corporate, sales, and personal income tax systems. We will find ways to close tax loopholes, promote efficiency in administration, enhance collection and enforcement, and simplify the tax code to improve New York's business climate, especially for small businesses."

I strongy recommend that property taxes be included under the pervue of the Commission. We cannot continue to look at taxes in a silo. No residents pay just sales and income taxes and no corporations pay just corporate taxes. If we are to fairly examine our tax structure we must look at it in its entirety.

Right now, according to an analysis from the Fiscal Policy Institute, we know that over 675,000 New Yorkers, with incomes under $100,000 per year, are paying over 10% of their income in property taxes. We also know that about a third of those same tax payers are paying more than 20% of their income in property taxes. To not include property taxes in the commissions purvue would be a disservice to the tax payers of NYS.

The charts below illustrate the need to include all state and local taxes when trying to determine tax burdens and issues of fairness within our current tax structure.

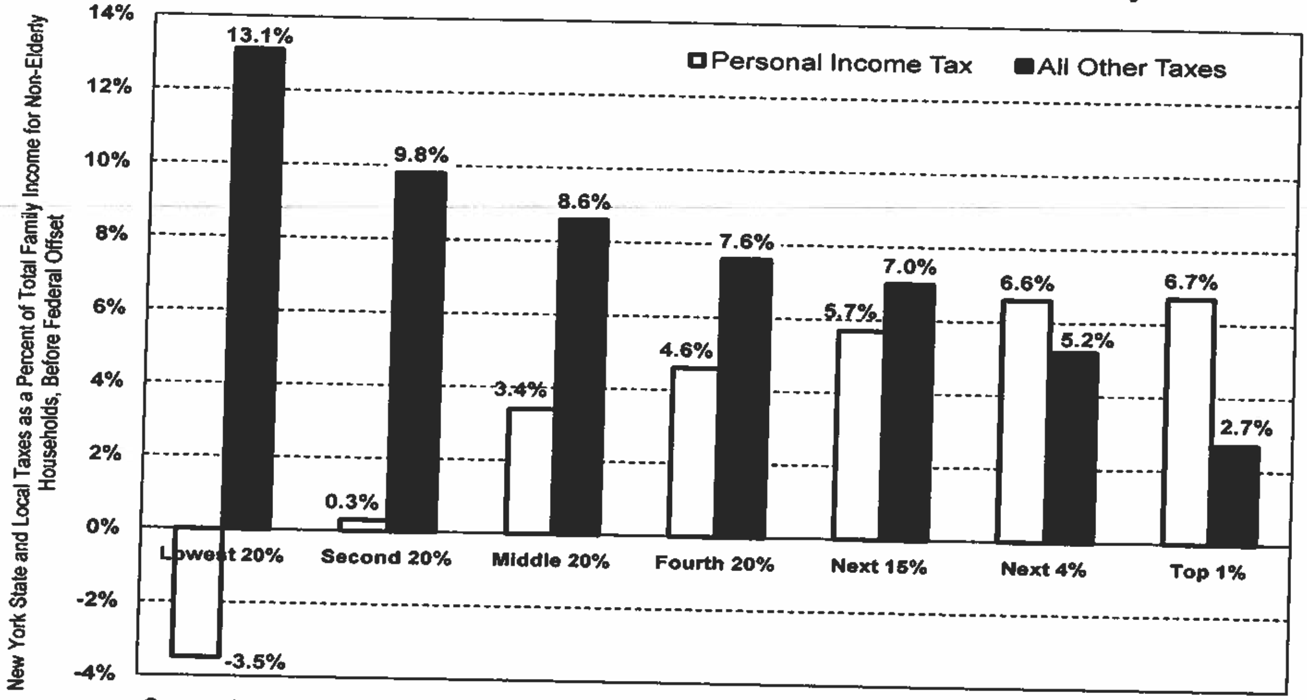
3. New York State & Local Taxes in 2007

Shares of family income for non-elderly taxpayers

Income group	Lowest 20%	Second 20%	Middle 20%	Fourth 20%	Top 20%		
					Next 15%	Next 4%	TOP 1%
Income range	Less than $16,000	$16,000 - $33,000	$33,000 - $56,000	$56,000 - $95,000	$95,000 - $209,000	$209,000 - $633,000	$633,000 or more
Average income in group	$9,600	$24,400	$43,800	$73,100	$133,000	$338,100	$3,065,800
Sales & excise taxes	**7.3%**	**6.0%**	**4.7%**	**3.7%**	**2.8%**	**1.7%**	**0.9%**
General sales - iIndividuals	3.6%	3.3%	2.8%	2.3%	1.8%	1.1%	0.6%
Other sales & excise - ind.	1.5%	0.9%	0.6%	0.4%	0.3%	0.1%	0.0%
Sales & excise on business	2.2%	1.8%	1.4%	1.0%	0.7%	0.4%	0.2%
Property taxes	**5.8%**	**3.8%**	**3.9%**	**3.8%**	**4.1%**	**3.3%**	**1.5%**
Property taxes on families	5.3%	3.3%	3.4%	3.4%	3.6%	2.6%	0.6%
Other property taxes	0.5%	0.5%	0.5%	0.5%	0.5%	0.8%	0.9%
Income taxes	**-3.5%**	**0.3%**	**3.4%**	**4.7%**	**5.8%**	**6.8%**	**7.0%**
Personal Income Tax	-3.5%	0.3%	3.4%	4.6%	5.7%	6.6%	6.7%
Corporate Income Tax	0.0%	0.0%	0.0%	0.1%	0.1%	0.2%	0.4%
TOTAL TAXES	**9.6%**	**10.1%**	**12.0%**	**12.2%**	**12.7%**	**11.8%**	**9.4%**
Federal Deduction Offset	-0.0%	-0.1%	-0.5%	-1.1%	-1.9%	-1.1%	-2.2%
TOTAL AFTER OFFSET	**9.6%**	**10.0%**	**11.6%**	**11.0%**	**10.7%**	**10.8%**	**7.2%**

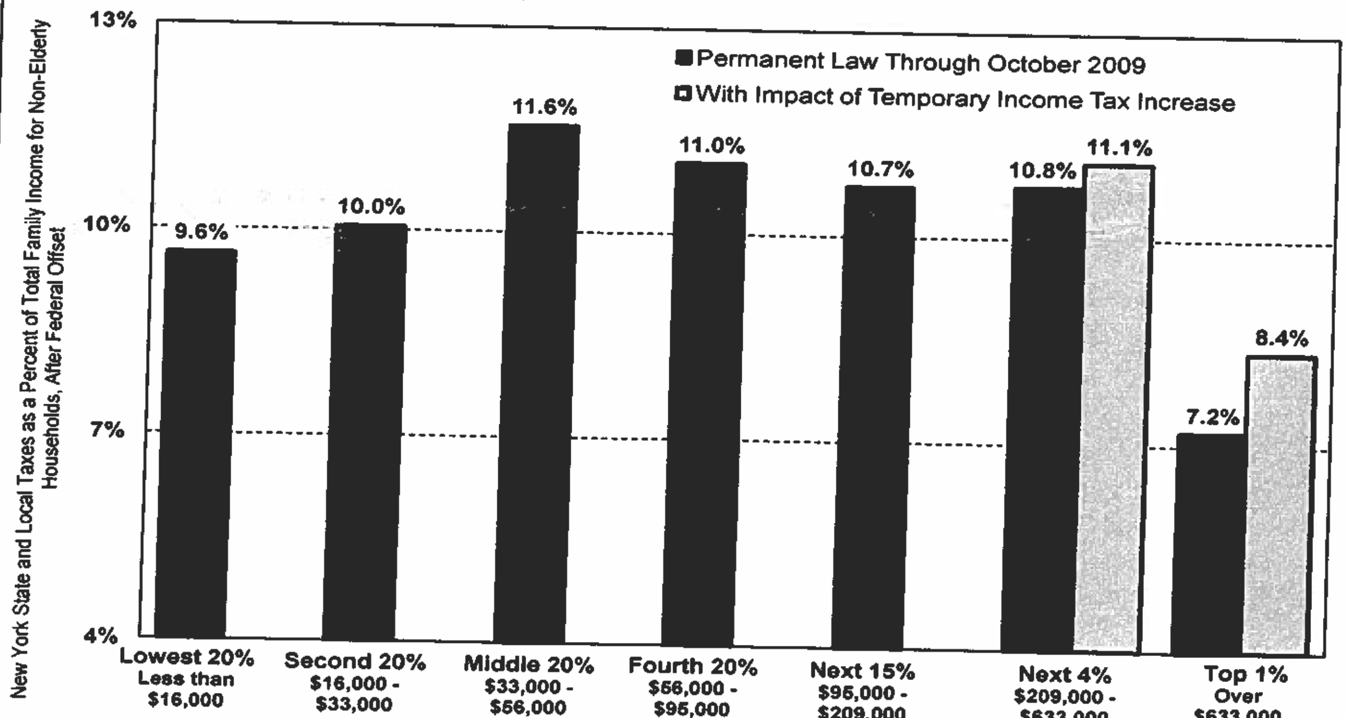
Note: Table shows 2007 tax law updated to reflect permanent changes in law enacted through October 2009.

4. New York's income tax is progressive, but not progressive enough to balance out the regressivity of the rest of the state-local tax system.



Source: Institute on Taxation and Economic Policy, 2009. Note: 2007 tax law updated to reflect permanent changes in law enacted through October 2009.

6. Overall, the wealthiest 1% of households pay a much smaller share of their income in state and local taxes than do all other New Yorkers, even with the temporary income tax increase.



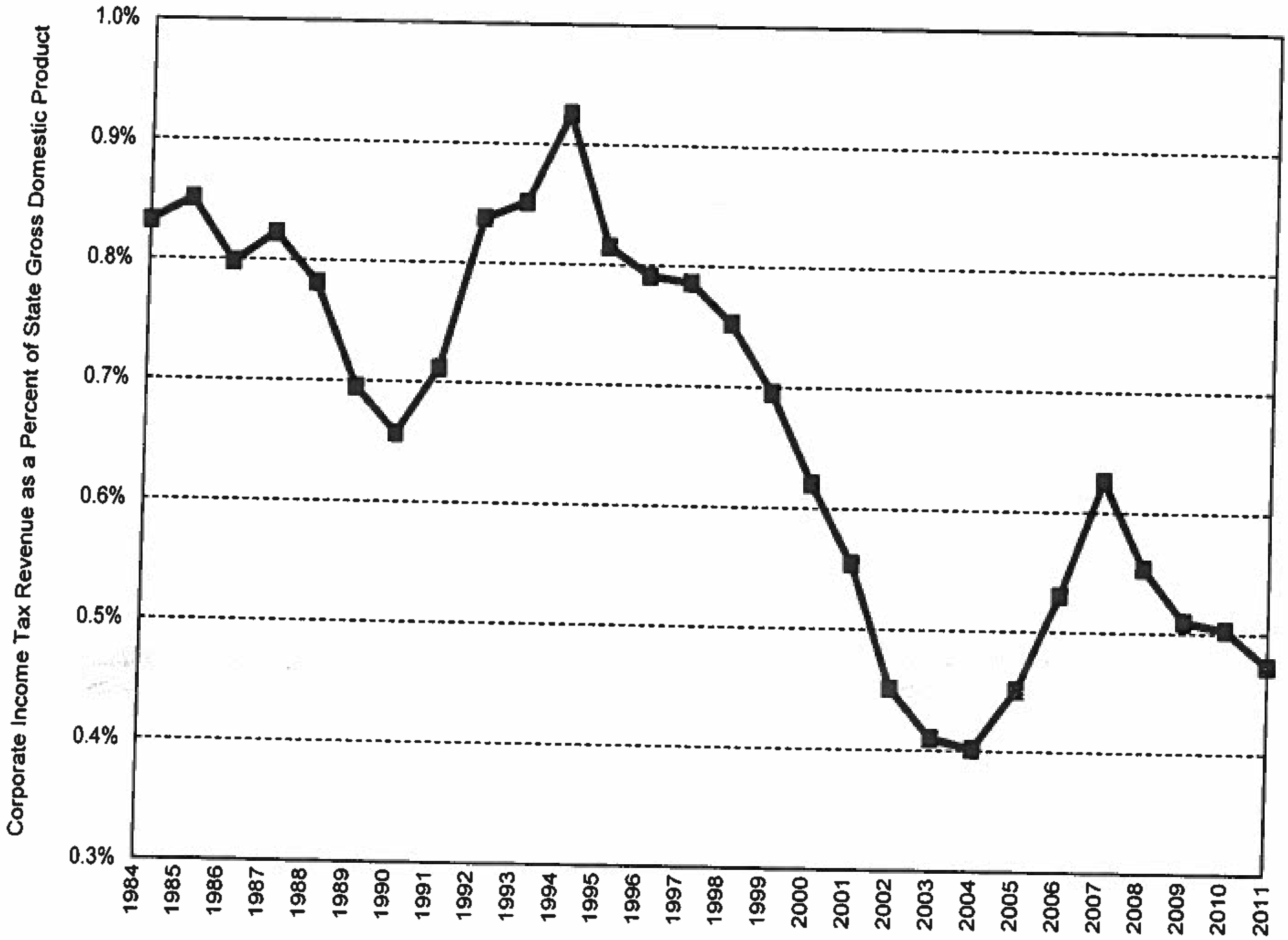
Source: Institute on Taxation and Economic Policy, 2009.
Note: 2007 tax law updated to reflect permanent changes in law enacted through October 2009.

Furthermore, I would recommend that the Commission not be bound to make "revenue neutral" decisions. If the Commission is to operate properly it should not be bound by politically motivated and predetermined outcomes.

<u>The Need for Corporate Tax Reform:</u>

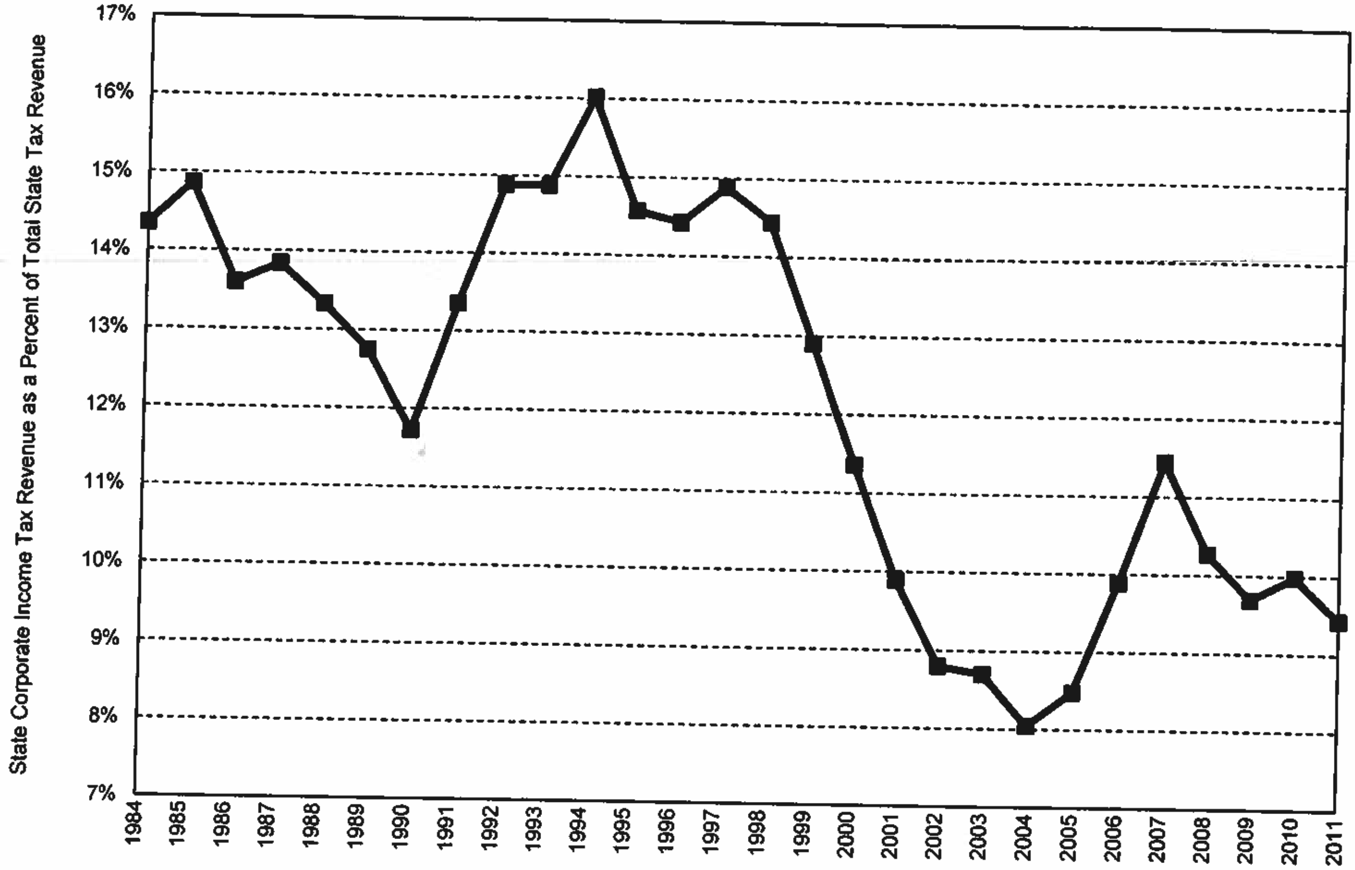
I believe that prior to the development of the tax commission we can take steps to immediately close some loopholes, create tax fairness and enforce our current tax laws adequately. The charts below from the Fiscal Policy Institute show how corporate taxes have fallen relative to the size of the state's economy and as a share of the state's total tax revenue.

New York's corporate income tax revenues have fallen substantially relative to the size of the economy.



Source: New York State Department of Taxation and Finance; U.S. Bureau of Economic Analysis (NYS GDP data).

New York's corporate income tax revenues have declined as a share of total state tax revenues.



Source: New York State Department of Taxation and Finance; U.S. Bureau of Economic Analysis (NYS GDP data).

I will discuss the reforms we are urging and group them using our three major principles: Enforcement, Fairness and Transparency.

Enforcement

Require Real Estate Partnerships To Pay The Taxes They Owe

New York must undertake a new intensive review of the tax returns of investors in real estate partnerships to ensure compliance with tax laws. In an examination of just one year's tax returns (2005), a former special agent for the IRS estimated that real estate investors underpaid $5 billion in taxes to the federal government and **$385 million** to New York State.

Underreporting or misreporting of capital gains from real estate investments is the main cause of tax underpayments. Reuters columnist David Cay Johnston, who reported the 2005 IRS data when he wrote for the New York Times, recently wrote that the annual underpayment of New York State taxes in connection with real estate partnerships ranged from **$200 to $700 million annually**. Johnston also pointed out that New York City alone could be losing out on $40 million annually.

New York could recover as much as $1 billion from prior-year audits, with annual revenues thereafter well over $100 million. The state of Pennsylvania recently discovered over $700 million in unreported gains and then made sure that the investors in Real Estate Partnerships paid the proper taxes on those overall gains.

Fairness

Reform New York's Corporate Alternate Minimum Tax (AMT)

Several significant loopholes that favor multi-state corporations were added to New York's Corporate AMT beginning in 1994 and the AMT rate was cut from 3.5% to 2.5% in 1999 and then to 1.5% in 2005 for non-manufacturers and most recently .75% for manufacturers (manufacturers rate was recently changed in the tax refrom package of December 2011).

These changes should be repealed or the AMT should be replaced with a variation of the Alternative Minimum Assessment (AMA) adopted by New Jersey in 2002. To ensure that such an assessment would *not* hurt small business, it should only be applied to businesses with annual gross profits of $5 million or more. We need to level the playing field between large and small businesses by making sure that large multinational corporations pay a minumum corporate income tax in NYS. NYS should increase the Corporate AMT to where it was a decade ago (3.5%) which would generate hundreds of millions in additional revenue.

Tax Nonresident Hedge Fund Management Fees

In his 2010 Executive Budget proposal, Governor Paterson proposed to "expand the nonresident personal income tax to include income received from hedge fund management fees."

As the governor's proposal explained, "Currently, only a small portion of such income is taxed as compensation, with the remainder deemed tax-free capital gains. This proposal would result in equal treatment of this income for residents and nonresidents." This proposal would generate $50 million in additional revenue.

Eliminate the Carried Interest Exemption Under New York City's Unincorporated Business Tax

The State Legislature should eliminate the carried interest exemption loophole in the New York City Unincorporated Business Tax, to put the taxation of private equity and hedge funds on the same footing as that of thousands of smaller businesses.

Right now, the UIB taxes fees received by managing partners in private equity and hedge funds but actually exempts profits from taxation. "Carried interest" is the technical industry term for the profit share received by managing partners (usually 20 percent of pooled investment profits) in hedge funds – anyone else would call it corporate profits.

The New York City Independent Budget Office estimated that eliminating the carried interest exemption for the Unincorporated Business Tax would yield $200 million a year for New York City. This reform was recently suported by Mayor Bloomberg at the federal level.

Transparency

Crackdown on Schemes that Create "Nowhere Income"

Multi-state corporations pay no taxes on profits attributable to sales made in states in which they do not have a physical presence. To address this situation, 28 of the 45 states with corporate income taxes, including California, Texas and Utah have enacted "throw-back" or "throw-out" rules to limit this drain on state revenues.

In contrast, New York actually went backwards on this issue in 2005, instituting a wasteful "Single Sales Factor" method for apportioning multi-state corporate profits that actually increase "nowhere income" and opportunities to evade taxes. It's time to institute reforms that have worked for other states.

Require Public Disclosure of Corporate Tax Payments for Publicly-Traded Companies

This proposal is revenue neutral, but disclosure and transparency measures are a good addition to any corporate tax reform package. We urge the state to adopt corporate tax disclosure for publicly traded firms subject to taxation under 9-A and 32 and any successor taxes. We need to know how much our state's corporations are actually paying in taxes in order to determine if it is too much or too little. Simply taking their word for it is simply not good enough.