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Before the Joint Legislative Fiscal Committees
February 9, 2015

Last year, as part of the fiscal 2015 budget, you approved New York's first permanent, broad-based state tax reductions and reforms since before the start of the Great Recession. The changes you made to the Corporation Franchise Tax and Estate Tax codes will help make New York a more attractive and competitive place to live, work and do business.

However, there remains much to do.

Looking ahead, the Legislature should consider tax policy options in the context of all the tax actions enacted by the state since the onset of the Great Recession.

In 2009 and 2010, New York raised taxes and fees by more than $7 billion. This was the largest such increase in our history, and one of the largest tax hikes enacted by any state in response to the downturn. On top of this, some $1.8 billion in new taxes and fees were imposed throughout the 12-county downstate region, where most of the state's personal and business income taxes originate.

An array of tax cuts enacted since 2011, many of them only temporary, have at least partially rolled back more than half the immediate post-recession increases. The state's tax burden has been redistributed, but not reduced. Personal income tax collections this year will continue to be at least $2 billion higher than they would have been under the permanent tax code, last in effect in 2008. The effective income tax rate – tax receipts as a share of personal income -- is well above the average level between 2002 and 2008.[1]

The most significant tax change proposed in Governor Cuomo's latest Executive Budget would create a new personal income tax credit designed to ultimately drive $1.7 billion a year in subsidies to roughly one million homeowners throughout the state, and a smaller number of renters, mostly in New York City.

The credit is supposed to serve as a "circuit breaker" for those whose property tax exceeds 6 percent of income, for homeowners earning up to $250,000. The biggest average savings inevitably will flow to residents of downstate suburbs, where property values are highest and taxes typically are a larger share of household income.

The credit also is likely to disproportionately benefit older, retired homeowners, who are most likely to be living on reduced incomes in homes that are worth many times what they originally paid for them. By the same token, senior citizens also are more likely to have paid off their mortgages, reducing their monthly expenses. In this sense, the proposal entails yet another form of intergenerational wealth transfer to retired persons from younger, higher-earning workers.

The state already funds a very significant homeowner property tax subsidy in the form of the $3.4 billion School Tax Relief (STAR) program, which provides added school aid to pay for partial homestead exemptions (and for across the board resident income tax cuts in New York City). "Enhanced" STAR benefits are available to most homeowners who are 65 or older.

The governor's budget also proposes changes to STAR that will cap the value of the tax break, convert it to a tax credit when a home changes hands, and eliminate any remaining STAR income tax break for New York City residents with incomes above $500,000 a year. These changes, combined with recently improved enforcement and administrative standards, are expected to reduce annual STAR outlays by a total of $280 million by fiscal 2019.

Nonetheless, if the governor's proposal is enacted, the state by 2018 will have not one but <u>two</u> homeowner property tax subsidy programs costing a total of nearly $5 billion a year. Both STAR and the proposed property tax credit are subsidies designed to treat a symptom rather than dealing with the underlying disease. You will be offering $1.7 billion in Band Aids on top of $3.1 billion worth of aspirin.

Instead of creating yet another big state property tax subsidy, the Legislature should instead reconsider a few basic questions.

If your policy goal is to provide across-the-board "relief" based on property values, then STAR remains the best approach.

If you aim to help only those homeowners who literally find their taxes to be "unaffordable," then a circuit breaker credit is the way to go.

But New York doesn't need both approaches—especially now that the property tax cap is clearly doing its job of holding down local tax levy increases, especially at the school district level.

The best way to help <u>all</u> local property taxpayers, homeowners and businesses alike, is to permanently enacting the property tax cap, whose fate is now tied to the continuation of otherwise unrelated rent control laws. Instead of creating new and superfluous tax breaks, the Legislature should consider other tax priorities that will do more to boost the competitiveness of the Empire State.

First, the governor's budget includes necessary technical corrections to the revised estate tax. This is an opportunity for you to repair a glaring problem still embedded in the law. Prior to last year's cut, New York taxed estate valued at more than $1 million. The new law will raise the tax exclusion, in stages, until by 2019 it reaches the level taxed by the federal government, which is now nearly $5.4 million. While New York will remain one of a dwindling number of states that impose any estate tax, this change will eliminate the tax on the lifetime savings and assets of hundreds of thousands of families, small business owners and farmers.

However, while last year's budget bill left the rate table intact, the final legislation also preserves outdated aspects of the old law, including a steep tax "cliff." The result, as one leading accountant and estate lawyer noted, is a confiscatory 164 percent marginal New York tax rate on estates valued at between 100 percent and 105 percent of the applicable federal exclusion amount.[2]

The technical fixes required as part of the next budget give you the opportunity to further revise the law so that New York's Estate Tax exclusion, like the one at the federal level, features a true tax threshold rather than a vertical cliff.

A second and much broader set of concerns is presented by the many loose ends in New York State's personal income tax code. In December 2011, the Legislature extended a significantly higher tax bracket for taxpayers earning $1 million or more (or above $2 million for joint filers), combined with rate cuts for married filers earning between $40,000 and $300,000, and a long-overdue provision "indexing" brackets to inflation. But all of these changes are temporary, set to expire at the end of calendar year 2017, within the four-year financial plan provided with this Executive Budget.

New York's high top income tax rate—among the highest imposed in any major state—is an economic negative because it creates a disincentive to work, save and invest here.[3] The personal income tax is an integral part of the business tax climate because a significant number of firms, including sole proprietorships, partnerships, and S corporations, are subject to this tax. New York's small businesses, in particular, would benefit from a more competitive and predictable income tax structure.

Economic considerations aside, fiscal stability is another substantial reason to begin planning a phase-out of the millionaire tax. Twenty years ago, at the end of Governor Mario Cuomo's tenure, the personal income tax represented 51 percent of New York's state tax receipts. In 2015, the personal income tax will comprise 63 percent of tax receipts—an all-time high. This is expected to rise even further, to 64 percent in 2017.

About 43 percent of PIT receipts now come from the top one percent of tax filers – individuals and couples whose incomes start at just under $1 million a year. This means that 27 cents out of every dollar the state collects from all tax sources will be generated by fewer than 100,000 tax filers, many of them business owners or investors.

There are clear risks associated with depending so heavily on such a small number of taxpayers. It means that when high-income households have a bad year, the entire state suffers inordinate fiscal stress. This is precisely what happened to New York between 2001 and 2003, and again to an even more significant degree between 2007 and 2009. Virtually all of the decline in tax revenues during those periods was concentrated in high-income households—and New York is now even more dependent on these taxpayers than it was before 2009.

In sum, the best way to build on last year's progress in reducing New York's tax burden would be to eliminate the confiscatory "cliff" in the reformed Estate Tax, permanently enact across-the-board currently temporary cuts in personal income taxes, and adopt a schedule for phasing out the temporary tax increase on highest-income individuals and businesses. And while it may not be an immediate budget issue, the best way to offer a promise of lasting property tax relief would be through the permanent enactment of the property tax cap.

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[1] See pp. 168-171 of the 2016 Executive Budget, *Economic and Revenue Outlook.*
[2] Kevin Matz at https://www.linkedin.com/groups/NEW-YORK-BUDGET-BILL-JUST-4471458.S.5855721452124282880?trk=groups%2Finclude%2Fitem_snippet-0-b-ttl
[3] For further discussion of the economic impact of higher income tax rates, please see the testimony at http://www.empirecenter.org/testimony/2009/03/EJMTaxTestimony31209.cfm