5 Steps to Reforming New York's Tax Code

How to Grow the Economy and Increase Competitiveness

A joint statement from:
Joseph Henchman, *Vice President for State Projects,* Tax Foundation
E.J. McMahon, *President,* Empire Center for Public Policy

December 4, 2013, Washington D.C.—In recent weeks, Governor Cuomo has signaled that he intends to pursue tax reduction and reform as a major priority in 2014. The Empire State's tax code is sorely in need of improvement, as indicated by New York's last-place ranking in the Tax Foundation's *2014 Business Tax Climate Index*.

Governor Cuomo has projected that maintaining a 2 percent cap on annual growth in state expenditures could lead to a budget surplus of up to $2.9 billion by fiscal year 2017. The key question, in his words, is "how do you use this period of growth to actually increase the economic competitiveness of the state of New York?"

Based on our analysis of New York's state and local tax structure, that question could be answered by addressing the following five initial tax policy priorities, which would not only make New York more business-friendly, but would reduce the high tax burden on all New York residents:

1. Immediately begin a phase-out of the temporary personal income tax increase on high-income earners, with the goal of reducing the top rate in stages from the current 8.82 percent to the permanent-law level of 6.85 percent by 2017;
2. Permanently enact the temporary middle-class income tax cuts first enacted in December 2011 and extended through 2017;
3. Permanently index the state personal income tax code to inflation;
4. Increase the exemption of the New York Estate Tax to match the federal level of $5.25 million; and
5. Permanently enact the 2 percent local property tax levy cap.

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 State's personal income tax—compounded in New York City's by an added resident income tax of up to 3.9 percent and an unincorporated business tax of 4 percent—currently suffers from high rates and narrow bases. Rolling back temporary personal income tax increases and making permanent the temporary tax cuts initially enacted in December 2011 would be important first steps towards necessary reform of the personal income tax code.

(more)

Additional resources to fund state tax relief could be made available by eliminating the state sales tax exemption for clothing purchases under $110, as recommended by the governor's Commission on Tax Reform and Fairness. This would free $800 million for permanent additional income tax reductions benefitting low and middle-income households. Further resources could be derived from canceling the Family Tax Credit, a temporary rebate scheduled for issuance for the first time in the fall 2014. The program has an annual budgeted cost of $410 million.

Further study should also be given to ways of reforming and reducing business taxes, as recommended by both the Commission on Tax Reform and Fairness in the preliminary report of the Senate Republican Tax Policy Reform & Review Initiative.

New York's property taxes consistently rank among the highest in the country. In the long run, the governor's 2 percent cap on local property tax levies should lower this tax burden. For that reason, it is important to remove any doubt of the cap's permanence by removing the conditional 2016 sunset date from the current tax cap law. Governor Cuomo has said he wants to follow up on this tax cap by enacting a "circuit breaker," which is the customary term for a personal income tax credit based on the level of property taxes paid as a percentage of a household's income.

However, in addition to a small circuit breaker enacted in the 1970s, New York State in fiscal 2015 is already slated to spend $3.6 billion on the School Tax Reduction (STAR) program, which is financed directly from personal income tax receipts. STAR consists of homestead exemptions in school districts throughout the state except in New York City, where it takes the form of a reduction in resident city income tax rates. Any new form of state-subsidized "property tax relief" would not constitute a net tax reduction, but would merely shift a portion of the burden from local property owners to state taxpayers.

Tax policy in New York should be guided by Governor Cuomo's declaration in his first State of the State message: "We have to hold the line on taxes for now and reduce taxes in the future. New York has no future as the tax capital of the nation. Our young people will not stay. Our business will not come. This has to change."

####

Contact:
Richard Borean, Tax Foundation, 202-464-5120
Tim Hoefer, Empire Center, 518-434-3100