Written Submission of the Fiscal Policy Institute
Joint Legislative Budget Hearing on Taxes
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The Fiscal Policy Institute is an independent, nonpartisan, nonprofit research and education organization committed to improving public policies and private practices to better the economic and social conditions of all New Yorkers. Founded in 1991, FPI works to create a strong economy in which prosperity is broadly shared.

Thanks to the economic recovery for certain sectors of the workforce and the tax increases in the FY 2022 budget, New York is entering FY 2023 with budget surpluses projected for the next five years. Yet the strength of the state's tax receipts conceals a highly unequal economic recovery from the COVID-19 pandemic. Many lower-income workers have not regained their jobs, while high earning professionals, many of whom experienced only minimal economic hardship during the pandemic, have benefited from a booming stock market and rising business profits. This "K" shaped recovery has been widely remarked upon, and must guide the state's fiscal priorities in FY 2023.

FPI recommends that the state take advantage of revenue growth and budget surpluses to make substantial public investments that will promote a stronger and more equitable economic recovery. Now is the time to expand funding for childcare, public education, and existing programs of poverty relief such as the New York State Earned Income Tax Credit (EITC) and the Empire State Child Credit. Addressing childcare policy is of particular importance, as the costs of childcare place an excessive financial burden on working families, and the early years of childhood remain outside of the support provided by the public education system.

In order to achieve these social policy aims, revenues must be sustained and governance of tax expenditures must be improved.

A. Sustaining Tax Revenues

In order to sustain the state's fiscal position going forward, FPI recommends a number of additional revenue actions. These will be necessary for fiscal stability as the $13 billion in

federal relief funds are drawn down, and to further increase investment in foundational public services.

1. Make Permanent the FY 2022 Tax Increases. New York's strong revenues in FY 2023 are in part thanks to the tax increases passed in the FY 2022 budget, which are scheduled to sunset by 2027. These rates should be made permanent, as they have neither hampered the economic recovery nor caused migration out of the state by high-income taxpayers.[1] The state should also impose a surtax on the long-term capital gains of high-income taxpayers, a proposal from last year's one-house budget proposal that was not incorporated into the final budget.

2. Reform the Taxation of Pass-Through Income. Most businesses are now organized as "pass-through" entities, which pay no entity-level tax on business income.[2] By contrast, corporations pay an entity-level tax on corporate income. Because of the expansion of limited liability to pass-through entities through the use of limited liability companies (LLCs), the traditional rationale for exempting pass-through entities from an entity-level tax is much weaker than it used to be.

    a. The state should consider increasing the filing fees for LLCs and partnerships, and develop options for transforming that fee into an entity-level tax on either business profits or gross receipts.

    b. The state should also consider imposing a surtax on high-income taxpayers who benefit from the 20% deduction from pass-through income that was enacted in the Tax Cuts and Jobs Act under section 199A of the Internal Revenue Code.

3. Decouple from Regressive Federal Tax Policy. New York has long recognized that many provisions of federal tax policy are unsound handouts to business interests, and has accordingly decoupled its own tax laws from those provisions of federal law. For instance, New York does not conform with the deduction for pass-through income mentioned above in section 2(b), or with the federal tax benefits for bonus depreciation.

    a. The state should complete the process of decoupling from Qualified Opportunity Zones, which was started in the budget legislation for FY 2022.

    b. The state should decouple from the federal tax benefits for owners of Qualified Small Business Stock, which permit the exclusion of up to $10 million of gain on the sale of a business.

4. Assess Options for Increased GILTI Conformity. The 2017 Tax Cuts and Jobs Act added a novel provision to federal law which targets multinational profit shifting to overseas jurisdictions. These rules ("global intangible low-taxed income" or GILTI) require a

[1] Robert Mujica: "We haven't seen any evidence of [tax migration]" January 18, 2022 https://www.youtube.com/watch?v=K0Tj5ogmEMY.

[2] According to the Brookings Institute, as of 2014, 95% of business were organized as pass-through entities. https://www.brookings.edu/research/9-facts-about-pass-through-businesses/.

corporation to include in income certain excess profits of foreign subsidiaries. New York currently excludes 95% of this amount from a corporation's calculation of its New York tax liability. The GILTI inclusion amount should be increased, and, as these rules are likely to change under proposals from the Biden Administration, options for apportioning a share of GILTI to New York should be devised.

5. Impose the Pied-à-Terre Tax. The prevalence of unoccupied luxury homes in the New York City real estate market has led to calls for more progressive property taxes on these units. The "pied-à-terre" tax would impose higher property tax rates on non-primary residences worth $5 million or more. FPI estimates that this tax could raise approximately $500 million in additional revenue.

B. Reforming Tax Expenditures

Raising revenue in a progressive manner is only one aspect of good tax policy. It is comparably important that tax exemptions and tax credits be used sparingly so that the tax base is preserved. When particular interests get tax breaks, the lost revenue must be made up by all other taxpayers. Broadening the tax base allows for lower tax rates overall, and prevents discrimination among similarly situated taxpayers.

Moreover, tax incentives are highly controversial, as there is little evidence of their efficacy in boosting economic growth. A 2013 study by New York's Tax Reform Commission states that "there is no conclusive evidence from research studies conducted since the mid-1950s to show that business tax incentives have an impact on net economic gains to the states above and beyond the level that would have been attained absent the incentives."[3] Rather than paying for ineffective incentive schemes, the state should fund core social spending programs such as public education and childcare. FPI recommends broadly pursuing the following policy agenda.

1. Phase Down Major Tax Incentives. New York spends hundreds of millions of dollars annually on its largest business tax incentive programs, including the Film Tax Credit, the Excelsior Jobs Program, and the Investment Tax Credit. Funding for these programs should be scaled down significantly, refundability of credits eliminated, and strict compliance controls put in place.

2. Enact Governance Reforms. Many sound legislative proposals have been made that address the ongoing concerns around economic development incentives, including expanding the "Database of Deals," expanding the funding and powers of the Authorities Budget Office, establishing an independent review board to assess incentives, and imposing clawbacks on beneficiaries of incentives that do not meet stated goals.

3. Reform the Powers of IDAs. Industrial Development Agencies, which are exempt from property tax, sales tax, and mortgage recording tax, are able to pass these benefits on to businesses. These benefits impose revenue losses on the state and violate basic principles

[3] Marilyn Rubin and Donald Boyd, 2013. "New York State Business Tax Credits: Analysis and Evaluation" http://www.capitalnewyork.com/sites/default/files/131115__Incentive_Study_Final_0.pdf

of tax policy. The powers of IDAs to grant tax breaks to businesses should be reevaluated and reformed.

4. Allow Section 421-a to Expire. The 421-a property tax exemption is New York City's most expensive tax expenditure program, costing the city $1.7 billion in foregone revenue for FY 2021. The 421-a exemption program should be replaced and redesigned completely to ensure that it produces meaningful affordable housing and is not merely a subsidy to developers. Beyond the lost revenue, the 421-a exemption increases the property tax burden for non-421-a landlords, who pass these costs on to their tenants.

C. Expanding Tax Credits

Tax credits are the primary mechanism for poverty relief in the United States. The Earned Income Tax Credit (EITC) and the Child Tax Credit are the major federal poverty relief programs, and New York has its own versions of these credits that piggyback on the administration of the federal credits. In light of the ongoing economic hardships faced by working families, now is the right time to expand direct payments through existing tax credit programs.

1. Expand the EITC to ITIN filers. Last year, New York ensured that undocumented workers who did not receive federal pandemic relief were still protected with the Fund for Excluded Workers. Going forward, the state should expand the benefits of the New York EITC to undocumented workers by allowing the credit for taxpayers who file with an individual taxpayer identification number (ITIN). California, Colorado, Maryland, New Mexico, Oregon, and Washington have all enacted this policy change.

2. Expand the Empire State Child Credit. For the same reasons that expanding access to childcare must be a legislative priority in FY 2023, expanding direct payments for the benefit of children is essential to the ongoing pandemic recovery for working families.