*Testimony to*

# Senate Finance Committee and Assembly Ways and Means Committee

***Joint Legislative Public Hearings on the FY 2013-2014 Executive Budget Proposal***

*Presented by*

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My name is Ken Pokalsky, and I am Vice President of Government Affairs for The Business Council of New York State, Inc. We represent more than 2,500 private sector employers of all sizes, in all industry sectors, across New York State.

The Governor, Senate and Assembly deserve credit for two very productive years in 2011 and 2012. Together, you brought state spending into line with our state's economic realities, you applied much need reforms to major state spending programs, and you took important steps in reigning in long-term public employee benefit obligations. You also made significant, substantial and necessary investments in public infrastructure and made additional economic development capital available.

For Fiscal 2014, we urge the Senate and Assembly to continue this progress and approve a final budget that maintains important fiscal reforms and reasonable controls on state spending. At the same time, we urge to look closely at several Executive Budget provisions, and adopt alternative approaches that will be more supportive of our shared objectives of renewed economic growth.

We still have important challenges before us in working together to make New York more economically competitive. We need to pursue opportunities to reduce regulatory hurdles that impede investment and job growth, and to lower overall business costs.

**Overview** - The Executive Budget for Fiscal 2014 proposes a modest increase in total state spending of under 2 percent and closes a $1.3 billion gap between projected revenues and spending.

On the downside, the budget proposal illustrates that New York's structural budget gaps persist. After a balanced budget for FY 2014, the state projects deficits for the following three fiscal years of $2.0 billion, $3.5 billion and $4.5 billion, respectively, for an aggregate three year gap of about $10 billion.

The good news, however, is that these gaps remain fairly manageable. As projected by the Division of Budget, continuing forward with budget growth in the two percent range should produce a modest budget surplus by FY 2016. That should be our shared objective.

Long term, though, renewed economic growth, driven by new private sector investment and jobs, is the only real means for improving the well-being of New Yorkers. A strong private sector economy will produce jobs and family incomes, and generate state tax revenues necessary for investments in education, social services and public infrastructure.

We need to improve the state's economic competitiveness in order to promote new private sector investment and the creation and retention of good paying private sector jobs – actions that will result in improved economic opportunity for all New Yorkers. Renewed economic growth will provide revenues necessary to finance essential government functions, and allow the state to re-invest in areas crucial to supporting private sector investment: transportation infrastructure, higher education and others.

Job growth in New York State has lagged behind national trends for the past two decades. New York grew at about half the national rate during the 1990's, about 60 percent of the national rate in the 2000's. Think of how much better New York's fiscal and economic situation be in today - with increased economic activity and the state and local tax revenues it would produce – if New York had only matched national job performance.

Reforms adopted in recent budgets, and carried forward in the current proposal, are important not only for bringing the state's fiscal house into order, but for improving New York's economic climate as well. More still needs to be done in reforming business regulatory programs and providing mandate relief for municipalities.

With that brief introduction, I would like to provide several key provisions in the Executive Budget, including those we support, several that we oppose, and additional reforms that we believe deserve legislative support.

- **Unemployment Insurance** – The Business Council supports the unemployment insurance reform package included in the Executive Budget. It presents a reasonably balanced approach, given the competing objectives of repaying federal UI loans, adopting cost-savings reforms and increasing the state's maximum weekly benefit.

A key objective for business is timely repayment of the state's UI debt to reduce overall business costs, and restoring the state's UI fund to long-term solvency. We are also interested in reforms that base eligibility and benefits more directly to a claimant's degree of connection to the labor market. The budget proposal addresses each of these objectives.

Most important, this bill is designed to expedite repayment of the state fund's $3.5 billion federal debt, and restore the fund to long term solvency. The proposal would repay this debt by 2017, instead of 2019 as projected under current law. Moreover, the bill will reduce the likelihood of future deficits by redefining "solvency" as having sufficient reserves in the state UI fund to pay benefits in a future economic slowdown, not merely a fund balance above zero.

The budget will increase UI taxes in the short term to expedite federal debt repayment. It does so in two ways. It increases the taxable wage base to $10,300 in 2014, and in several steps to $13,000 by 2026 – changes that have the same proportional impact on all employers' UI tax payments. It also eliminates the six lowest tax brackets in the state's UI tax table, raising the tax rate for the best experienced-rated employers to from 0.9% to 1.5%. This is our largest concern regarding the proposal - its proportionally higher tax increase on employers with the highest category of positive experience rating.

EXAMPLE OF IMPACT ON EMPLOYERS

| | Positive Balance Employer | Negative Balance Employer |
|---|---|---|
| Current Law | $8,500 x 0.9% = $76 per job | $8,500 x 8.9% = $756 per job |
| Proposed Law | $10,300 x 1.5% = $155 per job | $10,300 x 8.9% = $917 per job |
| Impact | $79 or 103% increase | $161 or 21% increase |

As the debt is repaid, and UI fund balance restored, employers will see automatic reductions in their UI tax rates, as a function of the design of the state's UI tax table.

To reduce costs, the bill would increase the earnings required to qualify for UI benefits to $2,100 in a claimant's high earning quarter, and $3,150 overall, during the prior year (up from $1,600 and $2,400, respectively), and base claimant's benefits on their average high earnings in two of the last four calendar quarters, rather than just the top quarter. The bill would also require a claimant to make at least two documented employment contacts per week, subject to random audit, among other changes.

The proposal also increases the maximum and minimum weekly benefits for claimants on a graduated scale. From October, 2014 through October 2018, the maximum benefit incrementally rises from $405 to $450. From October, 2019 through October, 2026, the maximum benefit incrementally increases from 36 percent of the state average weekly wage to 50 percent.

However, to avoid a return to federal borrowing, the bill provides that, effective 2017, maximum benefits would not increase in any year when private sector jobs decrease in each of the first six months of a calendar year, or if the fund does not have sufficient resources to pay for scheduled benefit increases.

Overall, The Business Council supports this reform package, as it focuses on achieving UI fund solvency, bases eligibility and benefits on a claimant's strength of attachment to the labor market, and bases future benefit increases on fund solvency.

**Workers' Compensation** – The Business Council supported the 2007 workers' comp reform package, recognizing that it was a careful balance of benefit increases and cost-savings reforms. The increases were front-loaded and "hard wired," but the cost savings were dependent on development and implementation of various regulations and policies. As a result of slow and incomplete implementation of reform measures, the cost of workers' compensation coverage rose steadily after the "forced" 20 percent premium reductions in 2008, and the system is more expensive now than pre-reform.

Therefore, we are encouraged that the Administration is seeking to revisit the 2007 reforms, and propose additional business cost savings as part of this year's Executive Budget. The $900 million in projected savings from the Executive Budget workers' comp package includes the following:

- $500 million in one-time savings for self-insured employers by releasing assessment reserves (as the basis for employer-specific Workers' Compensation Board (Board) assessments shifts from indemnity to "pure premium," accounting rules say you no longer have to reserve for future assessments.)

- $300 million in annual savings on the elimination of the re-opened case fund (Section 25-a assessments.)

- $100 million annual savings in "aggregate trust fund" relief, applicable to commercial carriers only and the employers they insure.

The Executive Budget also includes a new program to help business (mostly small businesses) deal with the aftermath of the default of twenty-three self-insured trusts. The Board, through the Dormitory Authority, would be authorized to issue up to $900 million in bonds, ultimately backed by the Board's new consolidated assessment, to help these defaulted trusts finance "assumption of liability" insurance policies for defaulted group self-insured trusts. While not specified in legislation, recoveries from former members of defaulted trusts (encouraged by the close out of liabilities and provision of full and final releases) would be the initial source of debt service. (Note: The budget legislation does not include any specific methodology for the Board's new integrated assessment, nor has a specific proposal been put forth by the Board. We believe an across the board "premium" based approach makes sense.)

In addition, we are working with the Board regarding additional regulatory reforms, including updating the much outdated medical/impairment guidelines related to scheduled loss of use awards, and establishing a presumptive start time for the durational limits on permanent partial disability awards (e.g., presumption that "maximum medical improvement" occurs no later than 2 years after the date of injury.)

These proposed statutory reforms, plus several key additional regulatory measures, will help moderate the increase in workers' comp system cost that are being driven by increased, indexed maximum benefits.

**Extension of Energy Assessments** – The Business Council strongly opposes the Executive Budget proposal to extend by five years the 2 percent "temporary" surcharge on the gross intra-state receipts of electric, gas and steam energy sales by public utilities. This surcharge, set forth in Public Service Law Section 18-a, is currently scheduled to sunset at the end of Fiscal 2014. In a state with already high state and local taxes, fees and assessments on energy – with roughly 25 cents of every dollar paid for electric power in New York State going to pay government assessments– we believe it is simply counterproductive to continue to add new and increased energy costs on state ratepayers.

We strongly opposed this surcharge when it was first adopted in 2009 – at a then-projected cost impact of more than $600 million per year. Importantly, after the provision passed as part of the FY 2010 budget, and legislators fully recognized the impact this would have on business and residential ratepayers, many told us they regretted their vote. Now is the legislature's opportunity to

reverse course, and say no to this extension of a $500 million per year energy tax.

Moreover, our review of the recent proposals to limit available CO2 allowances under the Regional Greenhouse Gas initiative would add nearly $1.6 billion to total electric power costs for New York business and residential ratepayers between now and 2020. While this assessment will return some $800 million to the state to support various energy efficiency and alternative energy investments, it acts like an inefficient tax collection measure, netting about 48 percent of total increased payments for the support of public programs. Moreover, these increased charges will promote the purchase of power from out-of-state generating station, further weakening the financial status of New York's fleet of base-load generating facilities.

The adverse impact of these dual cost drivers – an extended 18-a assessment and limitations on available RGGI allowances – will be significant. We urge the legislature, and Administration, to reject both proposals.

**Minimum Wage** – The Executive Budget's proposal to raise the minimum wage to $8.75 per hour is well-intentioned legislation with unintended, adverse impacts.

In our already slow economy, the last thing New York needs is another state-imposed cost on business. Raising the minimum wage would impose $3,120 in direct costs per full time employee, annually. Add in employer costs for Social Security, Medicare, unemployment insurance and workers' comp that goes hand-in-hand with higher rates of pay, the total cost per employee is more than $3,300.

For a small business with a handful of employees, these costs add up fast, especially with the economy producing little in the way of new sales. To accommodate these increased costs, business have limited choices: increased prices, divert resources from other purposes, attempt to become even more "efficient," or purchase less labor, meaning reduction in hours or elimination of jobs for some workers.

As for low-wage employees, a recent study by Cornell and American University shows this bill would hurt the very people who the proposal is intended to protect. It estimates that a minimum wage increase of $7.15 to $8.25 an hour (which is even less than the 21 percent hike proposed in the Executive Budget) would cost a total of 28,990 jobs in New York. A report by the U.S. Chamber of Commerce also indicates a negative relationship between minimum wages and employment, showing secondary impacts, such as a reduction in the amount of training provided to low-income employees, which would result from increasing the minimum pay rate.

The Business Council believes that the state's long-term future requires renewed economic growth in high-value sectors. Between 2000 and 2010, New York suffered a massive loss of middle and upper-middle income jobs – and the tax

revenues that go with them. Over this period, the state lost 496,000 jobs in the state's top paying private sector occupations. These sectors pay high salaries – $60,000 and higher on average - and produce significant tax revenues and economic spin-offs.

Going forward, New York needs to make the state more attractive for private-sector investment in higher wage occupations. Enacting legislation to raise the minimum wage, however, would serve as yet another tax on small businesses, retailers, the hospitality industry, farms and not-for-profits who are already struggling to stay afloat and keep New Yorker's working.

**Sales Tax Abatement for IDA-Assisted Projects** – We oppose provisions in the Executive Budget that would prevent industrial development agencies from granting state sales tax abatements unless, a) a project meets the eligibility criteria for Excelsior tax credits (regardless of whether they receive, or even apply, for Excelsior), and b) the abatement is approved by both a regional economic development council and Empire State Development. It also changes the form of this incentive from a point-of-purchase sales tax exemption to an after the fact tax refund.

We have several concerns with this proposal. First, smaller projects, and projects in categories excluded from Excelsior, would be categorically denied state sales tax abatement, regardless of the value of the project to the local community, and its consistency with REDC-developed strategic plans. For many projects, local IDA support is the most important incentive package available. Second, this proposal adds extra time and uncertainty to proposed investment projects.

With the sunset of Empire Zones, and adoption of a more targeted Excelsior tax credit program, the relative importance of IDA financing and tax abatement in local economic development efforts has increased, as they represent the principal remaining incentive tool for many types of projects. For these reasons, we do not support these proposed limitations on, and new procedural requirements for, IDA awarded sales tax abatements.

**Excelsior** – At the time of its adoption, The Business Council raised several concerns regarding the Excelsior program, including the relatively limited resource being dedicated to New York's flagship statewide economic development programs, its tight and - in some instances - mismatched eligibility criteria, its discretionary nature (as opposed to as-of-right credits), as well as expected implementation hurdles endemic to a capped tax credit program.

Recent public data showed that about 130 businesses were awarded Excelsior credits, with $184 million in current and future tax credits supporting nearly $2 billion in capital and research expenditures and nearly 14,000 new jobs.

Based on our discussions with ESDC, it is our understanding that, on average, Excelsior program participants have been awarded about 40 percent of the maximum credits for which they are eligible under Excelsior.

For these projects, this data speaks to both the efficiency and effectiveness of Excelsior deployment by ESDC. The state is producing real economic benefits, and doing so with an efficient use of state resources.

Economic development programs are always subject to the "but for" test, and concerns about "over incentivizing" projects. For these agreed-to projects, ESDC and the project sponsors have been able to come to agreement on incentive packages sufficient to promote new investment and job creation in New York State. And that is great news for the state.

What we do not know is whether and to what degree the Excelsior program's statutory limitations have resulted in missed investment opportunities.

Public data also indicates that in its first two years, including the soon-to-be completed 2012 year, less than half of the available Excelsior credits have been awarded to business. We appreciate that in year one, this low allocation level was due in part to normal startup hurdles. In addition, weak economic conditions also limited the number of businesses looking to make new investments and add jobs.

But Excelsior was designed to work like a grants program, implemented through the tax code, and unlike most capital grants program we can think of, Excelsior tax credit capacity that is unused in a given tax year is lost forever to the program.

Our first recommendation to the legislature is to modify Excelsior to allow for the carry-forward of unused Excelsior credit capacity to future tax years.

Our second recommendation is that, since ESDC retains full discretion to award Excelsior credits and to determine the level of credits available for any particular project, the program's eligibility criteria should be modified to provide ESDC greater flexibility, and result in a more useful development tool for the state. As the program would continue to apply overall cost-benefit tests, we believe this expanded flexibility and discretion would allow ESDC broader negotiating authority.

We also continue to call for repeal of the provision in Excelsior that requires a participant to forego tax credits previously earned for prior investments and job growth under the Empire Zone program, in order to qualify for any Excelsior credits. While we agree with long established statutory provisions precluding double credits for a single act, this feature of Excelsior makes no sense, if there are two wholly separate investments and job creation activities that serve as the basis for Empire Zone and Excelsior benefits, respectively. The law should be reformed to preserve tax credits already earned, and to be fully effective in promoting new investments and job creation.

Excelsior is off to a good start, given its limited resources, and we believe the program can be made more attractive for business looking to invest and grow in New York State, and more beneficial to the state and its residents.

**Tax Credit Deferrals** - In the 2010 session, business tax credits above $2 million per year per taxpayer were deferred for tax years 2010, 2011 and 2012 for most business incentive programs (key exceptions being Excelsior and the film production credit). These deferrals denied businesses the tax benefits promised them by the state for already-implement capital investments and job creation actions. In some instances, these deferrals imposed significant hardship on project-specific financing efforts.

The 2010 legislation that impose these deferrals also adopted separate schedules for the recovery refundable and non-refundable credits, respectively, beginning with tax years starting January 1, 2013. Importantly, the impact of these credit restorations is already included in the state's fiscal plans for FY 2014 and beyond.

The Business Council urges the legislature to support the timely recovery of these deferred business credits. We strongly opposed the initial deferral legislation, and will oppose any proposal to delay the recovery of deferred tax credits.

**Conclusion** - The Business Council of New York State supports Governor Cuomo's plan for fundamental changes in how New York State develops its budgets, and for advancing innovative approaches to managing State government.

Controlling spending will forces us to make programs more efficient - and likely more effective at the same time – and will help produce an economic climate that will support restored economic growth with new investment and jobs.

We believe the Executive Budget continues the new direction established over the past two budget cycles, and provides the right blueprint for the future of New York State. We urge the state legislature to adopt its general parameters, while addressing the issues highlighted above that will help improve the state's overall economic competitiveness.

That concludes my formal testimony, and I look forward to any questions or comments you may have.