Balancing New York State's 2004-2005 Budget in an Economically Sensible Manner

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Introduction and Overview

- The Fiscal Policy Institute (FPI) was established in early 1991 as an outgrowth of a broad-based "Coalition for Economic Priorities" that had come together two years earlier in response to the 1989-90 Executive Budget in which Governor Cuomo was proposing to close a $2.7 billion budget gap through deep cuts in important government services, increases in fees and regressive taxes and shifts in responsibility to local governments. Governor Cuomo insisted that the state balance its budget without increases in what he referred to as the state's broad-based taxes.

- In 1989, the Governor and the Legislature, despite or perhaps because of the state's fiscal problems and its weakening economy, insisted on going forward with the third phase of the large, multi-year personal income tax cut that had been enacted in 1987. Despite the claims that some advocates make regarding the relationship between jobs and broad based taxes, the large personal income tax cuts that were implemented in 1987, 1988 and 1989 did not innoculate New York from the emerging national recession. In fact, New York and the rest of the Northeast were hit particularly hard by that recession - and New York went from positive, but weakening, employment growth in 1989 to employment declines during each of the next three years.

- Beginning in 2001, after seven years of substantial tax cuts, New York State was again confronted by significant economic problems and related fiscal challenges. The 2002-2003 budget avoided significant tax increases and service cuts through the use of one-shots and the various reserves that the state had accumulated during the earlier boom times. In January 2003, however, the chickens came home to roost as Governor Pataki announced that the state faced an $11.5 billion deficit.

- In his 2003-2004 Executive Budget, the Governor offered a plan for balancing the budget that was very similar to the strategies that the state had utilized in the early 1990s - relying much more heavily on service cuts than revenue increases, and proposing increases in fees and regressive taxes rather than in taxes more closely related to the ability to pay. Last year, however, the Legislature modified the Governor's proposals in ways that substantially reduced the negative effects on the state's economy.

- This year's projected budget gap ($5.1 billion) is less than half the size of last years but in percentage terms the Governor is once again proposing a gap closing plan that relies more heavily on service cuts and cuts in state aid than is economically sensible.

- This briefing will review the roots of the budget gap that the Governor announced last January and which this year's budget continues to address. It will then compare the Governor's strategy for balancing the 2003-2004 budget and the alternate approach adopted by the Legislature, and review both the overall economics of the Governor's plan for balancing the 2004-2005 budget and some specific aspects of the Governor's budget that raise important fiscal and economic policy questions.

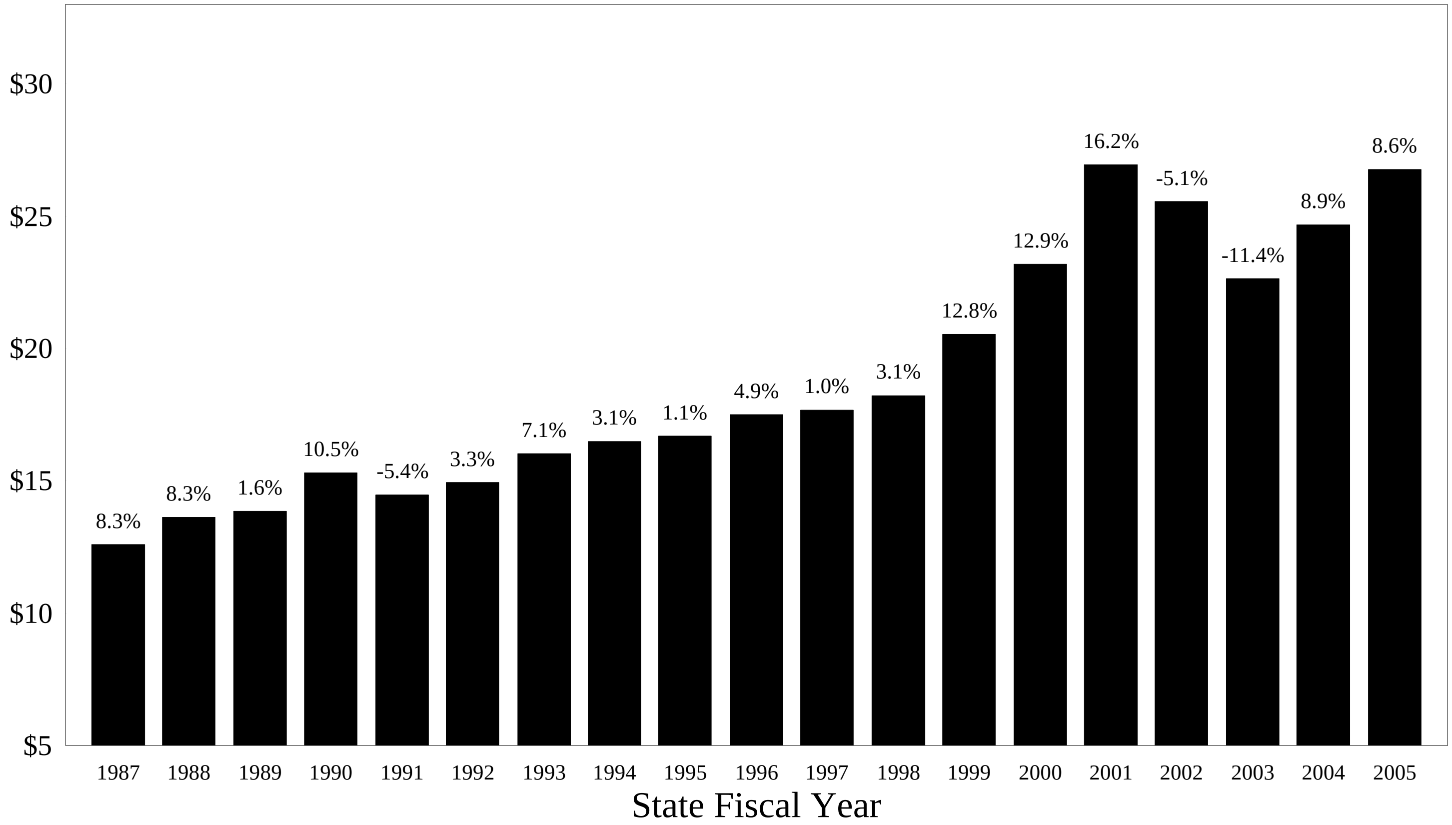
Origins of New York State's Budget Gap

- **The bursting of the Wall Street and dot.com bubbles**
- **The September 11th attacks and their aftermath**
- **The national recession**
- **An overly ambitious multi-year tax reduction that could not be sustained through a downturn in the economy or on Wall Street. But we got both and September 11th as well.**

  - **The bursting of the Wall Street and dot.com bubbles.** New York's 2003-2004 and 2004-2005 budget gaps did not emerge out of the blue in late 2002 or early 2003. The primary cause of these budget problems (and the budget problems facing most of the other states, as well) involved the bursting of two interrelated bubbles: the Wall Street bubble and the dot.com bubble. We now know that these developments hit the states like a tidal wave in 2001 but it is not clear when state officials were first aware of their actual impact on state revenues.
  - Beginning with the 1999-2000 state fiscal year, personal income tax receipts grew by double digits for three straight years: 12.5%, 12.7%, and 16.2%. This growth compensated for the cuts that were then being implemented in the states other less "elastic" taxes, allowing total revenues to grow sufficiently to finance several major programmatic expansions - particularly the state financed STAR homestead exemption which has grown to $2.8 billion from $0 in 1997-98, the expansion of Child Health Plus and the establishment of Family Health Plus - without significant reductions in other services.

The growth in the personal income tax base, primarily attributable to capital gains and Wall Street wages, compensated for the deep cuts in other

PIT collections in billions, for all funds, before cash management transactions. Percent change from previous year shown on top of each bar.



Source: The information for 1987 through 2003 is from Comptroller's Annual Report to the legislature. The information for 2004 is an estimate from the Executive Budget. The data for 2006 is a projection from the Executive Budget.

C But the bursting of the Wall Street and dot.com bubbles caused capital gains, the fastest growing component of personal income, to not only stop growing but to decline precipitously. This phenomenon did great fiscal damage not only to New York but to all the states with income taxes. In California, for example, taxable capital gains grew from about $20 billion a year in the early 1990s to $118 billion in 2000. But this source of income then plummeted to $48 billion in 2001 and $40 billion in 2002.

C In New York, the net amount of capital gains taxable on New York State personal income tax returns fell 52.7 % from $62.3 billion in 2000 to $29.5 billion in 2001, and another 33.5% to an estimated $19.6 billion in 2002. Governor Pataki's recently submitted Executive Budget estimates that this component of income fell another 6.5% to $18.3 billion in 2003 but that it is likely to increase to almost $21 billion in 2004.

C The result was a significant reduction in New York State's personal income tax receipts from a peak amount of $26.9 billion in 2000-01 to approximately $25.6 billion in 2001-02 and $22.6 billion in 2002-03.

C In last year's Executive Budget, the Governor estimated that personal income tax receipts would be approximately $23 billion during both the 2002-03 and 2003-04 state fiscal years. Receipts for 2002-03 (i.e., the fiscal year that ended on March 31, 2003) turned out to be a little less than projected - $22.65 billion, actual, vs. $22.9 billion, as estimated January 2003. Receipts for the current fiscal year (2003-04) are now being estimated by the Division of the Budget to be greater than last year's forecast for this year - $24.7 billion vs. last year's estimate of $23.1 billion. This is partially due to the economic and financial markets recoveries and partially to the temporary high-end rate increases adopted by the Legislature last Spring.

C After declining for two consecutive years, personal income tax receipts are again growing and are projected to be $26.8 billion in 2004-05.

Wall Street pay and stock market-related capital gains accounted for nearly two-fifths of the growth in New York's taxable personal income base, 1995-2000, but declines in 2001 and 2002 caused taxable income to fall.

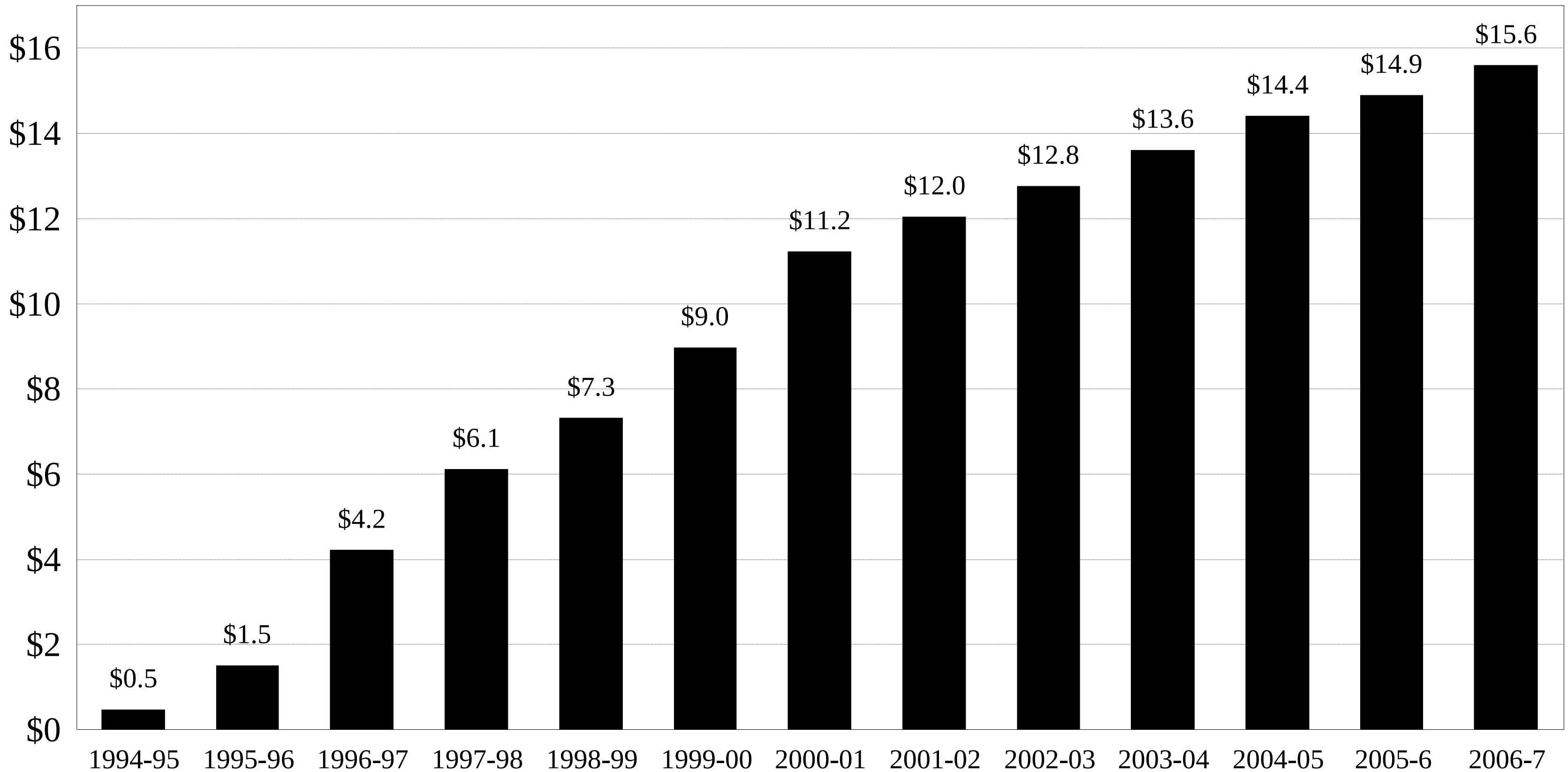
	Adjusted Gross Income (AGI) ($ millions)	Net Capital Gains ($ millions)	Total Wall Street Wages ($ millions)	Change from prior year			Capital Gains and Wall Street Wages as share of AGI	Capital Gains and Wall Street Wages share of AGI Growth over Prior Year
				AGI ($ millions)	Capital Gains ($ millions)	Wall Street Wages ($ millions)		
1991	$276,058	$8,735	$12,321	-7,369	-392	12,321	7.6%	
1992	$294,861	$9,457	$17,850	18,803	722	5,529	9.3%	33.2%
1993	$297,112	$13,365	$18,572	2,251	3,908	722	10.7%	205.7%
1994	$301,362	$12,032	$17,274	4,250	-1,333	-1,298	9.7%	-61.9%
1995	$321,124	$14,086	$20,187	19,762	2,054	2,913	10.7%	25.1%
1996	$347,891	$22,441	$24,534	26,767	8,355	4,347	13.5%	47.5%
1997	$383,179	$31,563	$28,790	35,288	9,122	4,256	15.8%	37.9%
1998	$417,996	$38,929	$33,602	34,817	7,366	4,812	17.4%	35.0%
1999	$453,130	$48,330	$35,116	35,134	9,401	1,514	18.4%	31.1%
2000	$519,501	$62,302	$48,777	66,371	13,972	13,661	21.4%	41.6%
2001	$487,532	$29,451	$49,810	-31,969	-32,851	1,034	16.3%	99.5%
2002	$467,119	$19,582	$40,081	-20,413	-9,869	-9,729	12.8%	96.0%
2003	$475,598	$18,312	$36,875	8,479	-1,270	-3,206	11.6%	-52.8%
2004	$502,290	$20,974	$40,378	26,692	2,662	3,503	12.2%	23.1%
change, 1995-2000	**$198,377**	**$48,216**	**$28,590**				**38.7%**	
change, 2000-2002	**-$52,382**	**-$42,720**	**-$8,696**				**98.2%**	
change, 2002-2004	**$35,171**	**$1,392**	**$297**				**4.8%**	

Sources: AGI and Capital Gains from New York State Division of the Budget; 2002-2004 are DoB projections. Wall Street wages from NYS Department of Labor; 1991-1999 on SIC basis, 2000-2002 on NAICS basis, 2003 and 2004 are projections by FPI.

- **The World Trade Center disaster.** No state suffered as much as New York from the September 11th attacks. State tax revenues were reduced by billions because of the loss of thousands of lives, the destruction of 26 million square feet of prime office space, and the indirect impact on numerous industries from hotels to apparel manufacturing.
- The U. S. General Accounting Office (GAO), in response to a request from U. S. Representative Carolyn Maloney and other members of New York's congressional delegation, reviewed and validated the Pataki Administration's estimate that $1.6 billion of the state's revenue losses during 2001-02 were attributable to the September 11th attacks. While the federal government has provided aid for other September 11-related losses, it has not yet provided any recompense for these revenue losses. At the time of its report on New York's revenue losses (http://www.house.gov/maloney/073002gao.pdf), the GAO said that it did not yet have enough information to reach a conclusion as to the reasonableness of the Pataki Administration's estimate of 2002-03 tax revenue losses attributable to the disaster.
- **The Multi-Year Tax Cuts.** In retrospect, it appears that the large multi-year tax cuts enacted in Governor Cuomo's last year in office and Governor Pataki's first six years were, when taken together, overly ambitious. The Division of the Budget estimates that these tax cuts are reducing state tax revenues by about $13.6 billion this year and $14.4 billion next year.
- Governor Pataki has described this effort as the largest multi-year tax reduction ever, by any state. In terms of balancing this objective with prudent fiscal planning, however, a tax reduction plan half this size would have still been the largest state tax reduction in history but New York would have been much better positioned to weather the fiscal storms of the last several years.
- Analysts and commentators who concluded that these tax reduction plans could not be sustained in the event of a downturn in the economy or on Wall Street, without significant backtracking on either the revenue and/or the expenditure sides of the budget, were dismissed as "nay sayers." Unfortunately, over the last several years, New York has had to deal with both of those development simultaneously <u>and</u> with the aftermath of September 11th as well.

The tax cuts enacted since 1994 will reduce state revenues by more than $14 billion during the 2004-05 fiscal year.

Revenue impact, in billions of tax cuts enacted in 1994 through 2003.



How the 2002-03 gap begat the 2003-04 gap

- All of these problems were clearly in focus in January 2002 when the Governor submitted his 2002-03 Executive Budget. At that time, the Governor estimated that New York State faced a $6.8 billion budget gap - $1.1 billion during the fiscal year that was then coming to an end and $5.7 billion during 2002-03. To get through the year, the Governor proposed some modest tax and fee increases, the use of approximately $2.6 billion in various reserves and other nonrecurring resources, freezes on spending for a wide variety of services and, in several areas, particularly in education and higher education, some pretty stiff budget cuts. The legislature restored many of the proposed cuts and provided an increase in school aid (which was still below the Budget Division's baseline). These restorations were financed primarily with the use of about $1.4 billion in additional nonrecurring resources.
- The situation at that time was that New York State was headed for a 2003-04 budget gap of at least $4.2 billion IF revenue growth rebounded as projected by the Governor in January 2002. <u>But it did not.</u> The result was the announcement in early 2003 of a budget gap of enormous proportions - $11.5 billion. This gap consisted of an estimated $2.2 billion shortfall for the 2002-03 fiscal year plus a projected budget gap of $9.3 billion for 2003-04.
- While the 2002-03 budget, as adopted, had anticipated a decline in revenues, the actual decline turned out to be about $2.2 billion greater than projected at the time of budget adoption. This meant that the state had to address a $2.2 billion gap in closing out its 2002-03 fiscal year. It also meant that the gap for 2003-04 would be at least $6.3 billion (i.e., $4.2 billion plus $2.1 billion) unless the rate of revenue growth was greater than the 5.25% projected in January 2002. <u>But it was not.</u> In reality, rate of revenue growth turned out to be less than previously projected, further increasing the projected gap for 2003-04 to the $9.3 billion level announced by the Governor in January 2003.

Executive Budget Proposals to Close the 2004-05 through 2006-07 Budget Gaps

($ Millions)

	SFY 2004-05	SFY 2005-06	SFY 2006-07
Projected Base Level Gap	$5,071	$6,727	$7,805
Total Spending Actions	$2,589	$2,495	$2,199
Total Revenue Actions	$972	$1,163	$1,118
Total Nonrecurring Actions	$1,510	$219	$139
Remaining Gap	$0	$2,850	$4,349

Closing the 2003-04 Budget Gap: The Governor's Approach

- On January 29, 2003, Governor Pataki proposed a multi-year plan for bringing the state's finances back into some semblance of structural balance. The Governor's multi-year strategy was not an illogical or inappropriate approach since implementing over $9 billion in recurring service cuts and/or recurring revenue increases during a single fiscal year could very well cause substantial harm to the state's economy. In thinking about the magnitude of this gap, it is important to remember that this gap was in the state's General Fund which, at the time, represented approximately $40 billion of state spending. (NOTE: Some General Fund gap closing actions can involve the use of resources from other funds.)
- Implicit in the Governor's multi-year approach were two kinds of budget balancing actions. **First,** the Governor was, in effect, proposing to reduce the projected budget gap to "manageable" proportions through one-shots (such as the proposed tobacco securitization), additional federal aid, efficiencies and other actions that would not create an additional drag on the state's economy during what was then a "job-loss" recovery.
- **Second**, in recommending a mix of more painful budget cuts and revenue increases to close the remaining gap, the Governor leaned much more heavily toward service cuts than to revenue increases; **and** in terms of the revenue increases that he did propose, he relied almost entirely on increases in regressive consumption taxes and fees.
- We said at the time and still believe that the Governor was correct in taking a multi-year approach to addressing the state's 2003-04 budget gap. And, in implementing such an approach, he was correct in proposing to reduce the projected budget gap to manageable proportions before resorting to service cuts and/or tax increases since these latter actions would create an additional drag on the state's economy. But, when it came to the mix of service cuts and tax increases that he proposed for closing the remainder of the gap, it was clear that much better choices were possible. And the Legislature ended up making a series of such "better choices" in the changes it made to the Governor's budget.

Executive Budget Proposals to Close the 2002-02 and 2003-04 Budget Gaps

($ Millions)

	SFY 2002-03	SFY 2003-04
Projected Base Level Gap	$2,200	$9,264
Tobacco Securitization	$1,500	$2,278
Spending Restraint/Administrative Savings Actions	$700	$5,638
Revenue Increases	$0	$1,348
Remaining Gap	$0	$0

	SFY 2002-03	SFY 2003-04
Spending Restraint Proposals		
Savings in school aid		$1,270
Medicaid cost containment		$1,020
State operations savings	$700	$1,000
Welfare savings		$587
Spending restraint in other local assistance programs		$977
Debt management actions		$516
Spending restraint in all other program areas		$268

Reducing the 2003-04 Budget Gap to Manageable Proportions

- The use of nonrecurring resources to balance the 2003-04 budget was criticized by some observers as "simply putting off the problem."
- But, attempting to close all or most of a $9.3 billion gap in a single year with ongoing service cuts and/or tax increases would have done significant damage to the state's economy.
- The argument that state policymakers should have “bitten the entire bullet" immediately was premised on the incorrect notion that the economy and Wall Street would not recover or that it would take many years for them to recover.
- The challenge in budgeting during such a period is guessing
  - guessing when these various recoveries are likely to begin,
  - guessing how strong they are likely to be, and
  - guessing what the effects (in terms of both timing and magnitude) they are likely to have on state revenues.
- On balance, the use of a mix of both recurring and nonrecurring actions to close the 2003-04 budget was not unwarranted even though uncertainty clearly existed at the time regarding the timing and strength of the recoveries in the economy and in the financial markets, and of their impact on state revenues.
- Under the Governor’s Executive Budget, the proposed tobacco securitization reduced the amount of the 2002-03 “close out” gap from $2.2 billion to $700 million, and the amount of the 2003-04 gap to be closed by other actions from $9.3 billion to $7 billion. Proposed debt restructuring and refinancing would further reduce the 2003-04 gap to be closed through spending cuts and revenue increases to a little less than $6.5 billion.

The Governor's Approach to the Hard Choices in the 2003-04 Budget

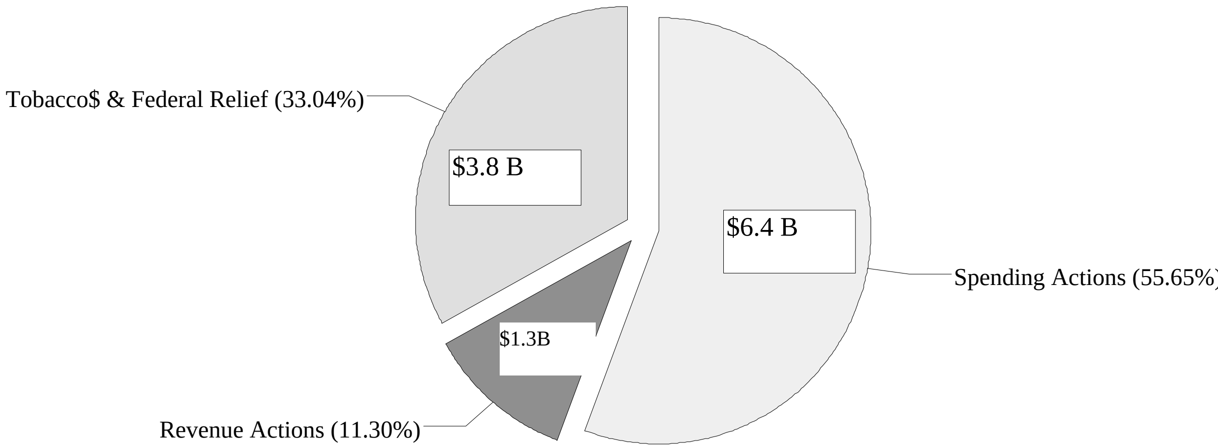
- Once the Governor got to the more difficult step of closing the remaining gap, he proposed to deal with the remaining $700 million gap for 2002-03 entirely on the spending side of the ledger and to cover the remaining 2003-04 gap with $5.2 billion in spending cuts and $1.3 billion in revenue increases, or about $4 of cuts (in state services and aid to localities) for every $1 of revenue increases.
- The revenue increases that the Governor did propose were overwhelmingly increases in consumption and other regressive taxes and fees. The largest single revenue increase proposed by the Governor, for example, involved eliminating the State's relatively new $110 clothing sales tax exemption and the replacing it with four one-week exempt periods.[1] Moreover, as the Governor's budget was reviewed by the Legislature and outside observers it became clear that many of the proposed cuts in aid to localities would have to be made up, at least in part, by property tax increases.
- The 2003-04 Executive Budget's $5.2 billion in General Fund spending cuts included a $1.27 billion cut in school aid, $1.02 billion cut in Medicaid, a $1 billion cut in other local assistance programs, a $1 billion cut in state government operations, and the use of over $500 million of federal family assistance funds to cover portions of the cost of the Tuition Assistance Program and other programs that were traditionally funded with state revenues.
- At the time, the Governor attempted to justify these policy choices by asserting a relationship among taxes, government spending and the economy that is inconsistent with basic economic principles, and presenting an incorrect rendition of New York State's economic history.

[1] In the adopted budget, the Legislature made the repeal of the clothing tax exemption temporary rather than permanent as proposed in the Executive Budget.

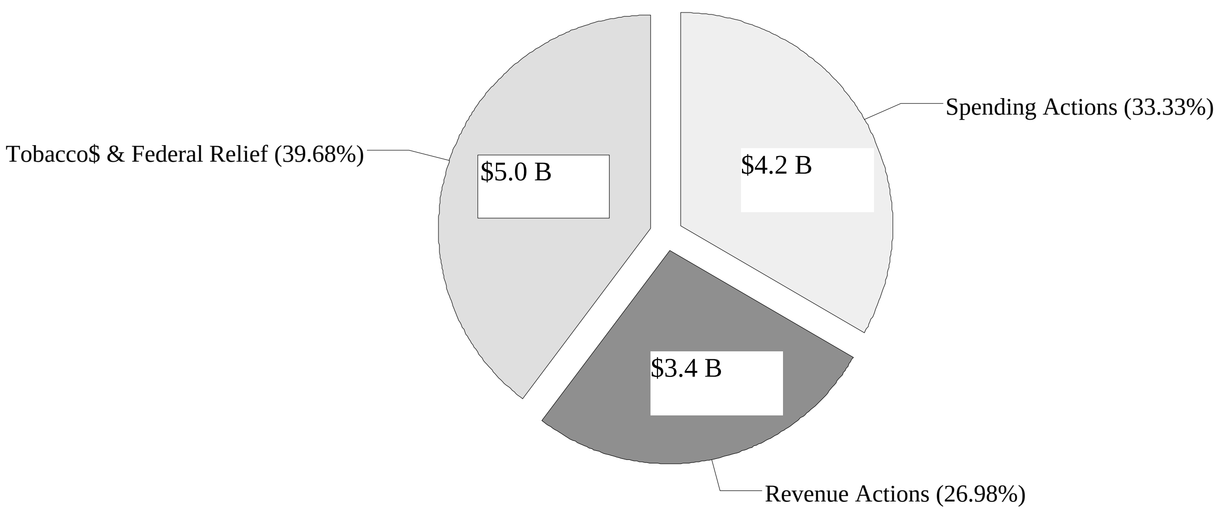
Closing the 2003-04 Budget Gap: The Legislature's Alternative

- In May 2003, the legislature adopted significant changes in the Governor budget bills. By that time, the 2-year budget gap had grown to $12.6 billion, due to revenue and spending re-estimates. Despite the growth in the size of the gap, the Legislature adopted a much more balanced approach to balancing the state budget, relying more heavily on revenue increases than the Governor had originally recommended and reducing many of the spending cuts that had been recommended by the Governor.
- Ten days after the original legislative passage of its budget package, the Governor vetoed the Legislature's bill to raise state taxes, authorize transitional borrowing and allocate school aid and line-item vetoed 118 spending additions. Within 20 hours, the Legislature overrode every one of the Governor's vetoes on a bipartisan basis.
- The Governor originally argued that the revenue increases enacted by the legislature would not cover all of its spending restorations. But, shortly thereafter, the Congress adopted a significant but temporary "state fiscal relief package." With this infusion of federal "budget balancing" aid, the Governor concluded that the 2003-04 state budget, as adopted, was credibly balanced.
- While much attention was focused on the Legislature's revenue actions, which included a temporary increase in the income tax rates for high income New Yorkers (the first income tax rate increases since 1971) and a temporary 0.25 % increase in the state sales tax, the Legislature, like the Governor, relied heavily on spending restraint to close the budget gap.
    - School aid was still $500 million below the baseline and about $200 million below the previous year's spending.
    - Spending on government operations and other local assistance was still $1.2 billion below the baseline.
    - State funding for SUNY was reduced by $183 million, forcing a $950 per year increase in tuition, the first such tuition increase since 1995.

Executive Budget Proposal



Enacted Budget



- C Many programs designed to help welfare recipients enter the labor force also suffered funding cuts. For example, funding to provide transportation assistance was cut by a third, from $7.5 million to $5 million; funding for Basic Education was cut from $5 million to $3 million and funds for drug abuse screening and treatment were cut in half (from $5 million to $2.5 million).

C The budget package adopted by the Legislature avoided the extremes that characterized the budget balancing packages of the early 1990s and the plan proposed by the Governor a in January 2003. The results to date have been heartening.

- C The Governor and his budget advisors are now estimating that New York will end the 2003-04 fiscal year with a surplus of several hundred million dollars and projecting the deficit for 2004-05 to be at the low end of their earlier projections ($5.1 billion).
- C In addition, the projected budget gap is overwhelmingly attributable to the multi-year strategy[2] that the Governor recommended for closing last year's $11.5 billion gap and which the Legislature adopted. Thus, for the most part, this is a "planned" deficit. That does not make it any easier to close but it does make it more understandable.
- C Since the adoption of the 2003-04 budget, the state's economic performance relative to the rest of the nation has improved. While both the state and national job creation rates for this period are extremely low, at least they are positive (a welcome turnaround from the first 18 months of the current "recovery") and New York is doing better than more than half the states.

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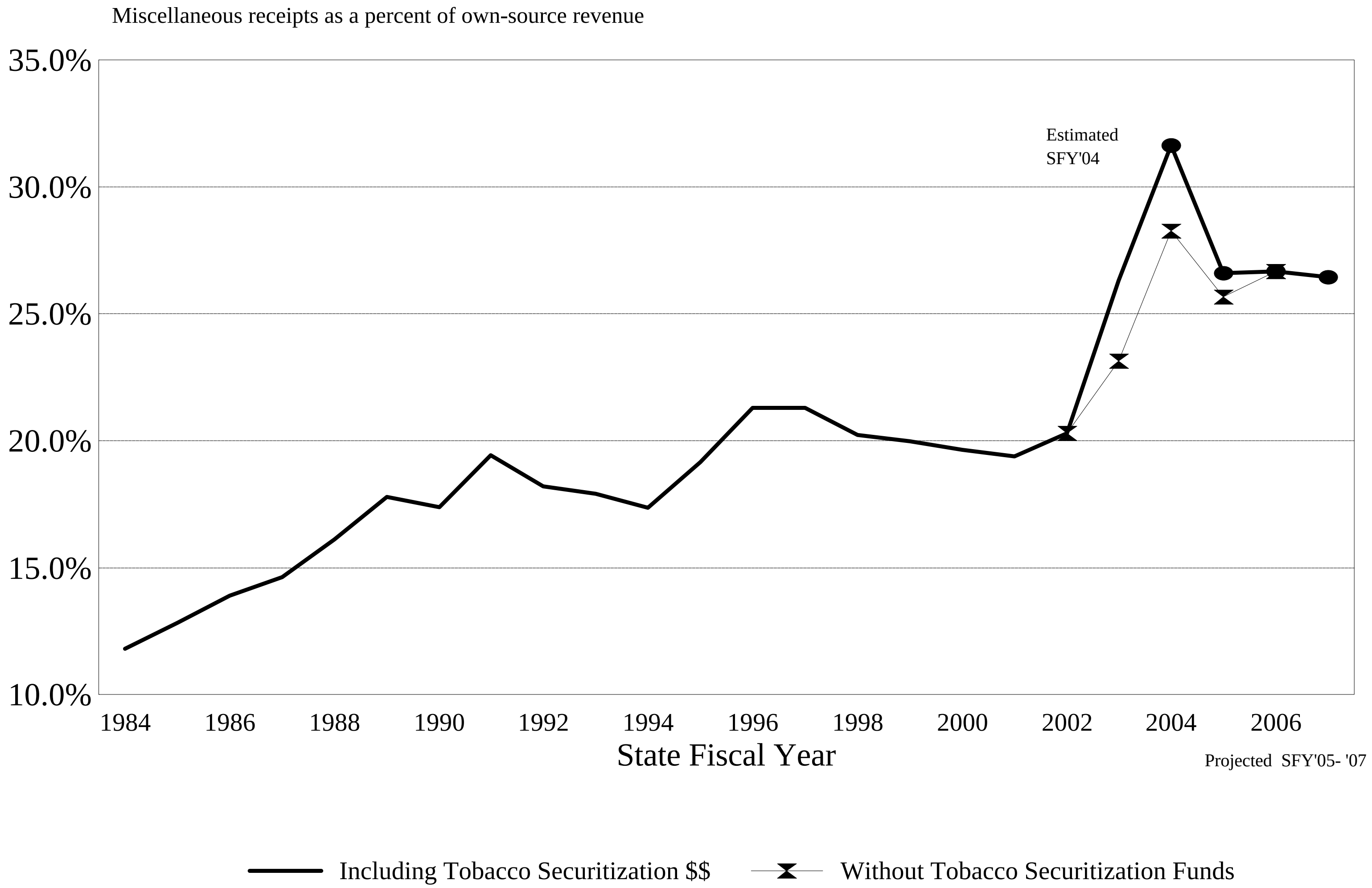
[2] The one-time actions that drive the projected $5.1 billion gap include the following, with the value of each as estimated by the Division of the Budget: Tobacco Securitization ($3.4 billion), temporary federal "fiscal relief" package ($1.035 billion), other one time revenues ($230 million), Medicaid Cycle Shift ($170 million), OMH Patient Income Account reserves ($220 million), TANF offsets ($568 million), TAP Spending roll ($104 million). After reducing the total of these one-shots by the one-time payments of $1.9 billion made in 2003-04 for 2002-03 bills, it appears that at least $3.8 billion of the $5.1 billion gap is a "planned" deficit resulting from the multi-year strategy used to close the 2003-04 budget gap.

Tuition, fees, one-shots, and other nontax revenues pay for an increasing share of services.

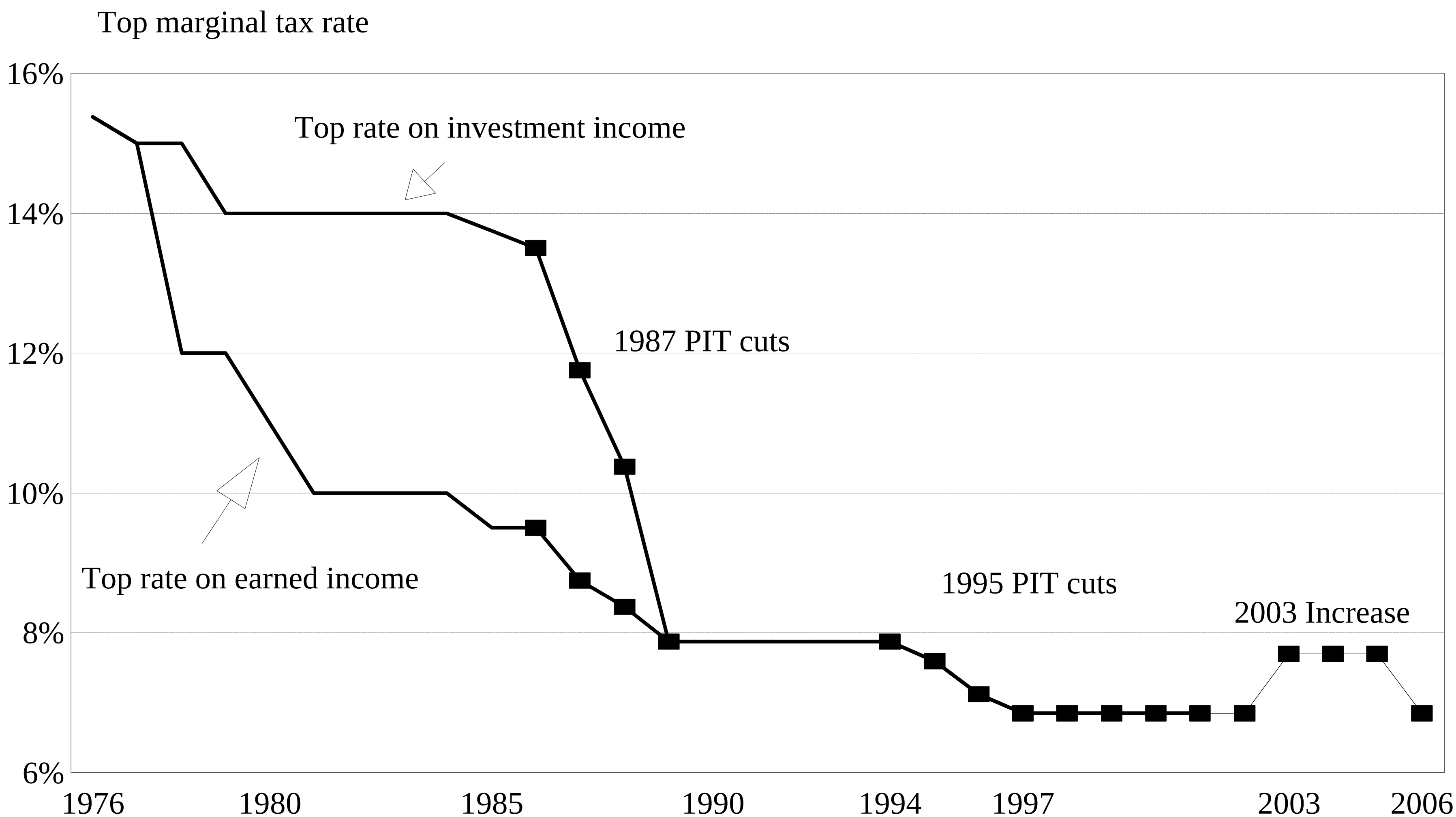


The 2003 Temporary Income Tax Rate Increases

The Effect on Taxpayers

- Through its action on the 2003-2004 budget, the New York State Legislature was able to greatly reduce the local property and sales tax increases and the service cuts that would have occurred if Governor Pataki's budget had been adopted as submitted.
- To a significant degree, this local tax relief was made possible by the Legislature's adoption of a temporary increase in the individual income tax rates for families with taxable incomes above \$150,000 and single individuals with taxable incomes above \$100,000. The legislature adopted two temporary brackets - one for taxpayers with taxable incomes between these levels and \$500,000, and the other for taxpayers with taxable incomes above \$500,000.
- The new top rate, which only applies to taxpayers with taxable incomes above \$500,000, is 7.7%. The second temporary rate was set at 7.5% for 2003, 7.375% for 2004, and 7.25% for 2005. The new 7.7% top rate is about half what New York State's top personal income tax rate (15.375%) was in the early and mid-1970s. And that top rate applied to the portions of taxable income above \$25,000.
- From a tax equity or tax fairness perspective, choosing a high-end income tax increase over further property and sales tax hikes was a positive step since it increased the effective tax rate for those taxpayers who pay less (relative to their income or ability to pay) in state and local taxes than the other 90% to 95% of New York taxpayers. *See* Appendix A for an explanation of the concepts of tax progressivity and tax regressivity and a summary of the findings of the most recent comprehensive analysis of the impact of the New York tax system on taxpayers at different income levels.

New York State has cut its top personal income tax rate by more than 50% over the last 25 years.



- Moreover, because state and local income taxes are deductible from income in calculating federal income tax liability, the net impact on affected taxpayers is much less than the amount of their additional payments to the state. In addition, the federal tax cuts enacted in 2001 and 2003 are particularly generous for taxpayers in these income ranges. The net result is that the combined impact of the recent federal, state and New York City income tax changes is a substantial net reduction in the income tax liability of affected taxpayers.

- Without even taking the President's cut in dividend taxes into consideration, the net tax cut for New York families earning $1 million is over $31,000 for those who live outside New York City and about $25,000 for those living in the city.

- New York families of four earning $300,000 a year (with an average amount of itemized deductions for that income level) will be paying about $8,400 a year less in income taxes in 2003 after taking into consideration both the federal and state tax changes. While such a family is paying an additional $1,737 to New York State, federal deductibility reduces the net effect of this tax increase by about 31% to $1,195.

- In 2004, this family's state taxes will decline by $400 as the second highest rate (applicable to taxpayers with taxable income between $150,000 and $500,000) declines from 7.5% to 7.375%. This temporary rate will decrease to 7.25% in 2005 and 6.85% in 2006.

- While the families in these examples are receiving the full benefits of federal deductibility, taxpayers with much greater than average itemized deductions would not because of the current structure of the federal Alternate Minimum Tax (AMT). Proposals have been made to change federal law in a way that ends the treatment of the deduction for state and local income taxes paid as an item of tax preference in the computation of federal Alternate Minimum Tax liability.

Change in Federal/State Tax Liability for a Family of Four

Based on Rate Increase From 6.85% to 7.5% for Taxpayers with Taxable Income between $150,000 and $500,000 and 7.7% for Taxpayers with Taxable Income over $500,000

	Adjusted Gross Income					
	$200,000	**$250,000**	**$300,000**	**$500,000**	**$1,000,000**	**$1,663,000**
2000 Federal Law						
Federal Itemized Deductions - 2000	$39,620	$53,595	$57,738	$80,824	$146,410	$224,971
Federal Exemptions -- 2000	$10,528	$6,048	$1,568	$0	$0	$0
Federal Taxable Income - 2000	$149,852	$190,357	$240,694	$419,176	$853,590	$1,438,029
Federal Tax Liability - 2000	**$37,575**	**$51,577**	**$69,698**	**$138,662**	**$310,690**	**$542,127**
2003 Federal Law						
Federal Itemized Deductions - 2003	$39,728	$53,698	$57,854	$80,965	$146,565	$225,138
Federal Exemptions - 2003	$12,400	$8,680	$3,720	$0	$0	$0
Federal Taxable Income - 2003	$147,872	$187,622	$238,426	$419,035	$853,435	$1,437,862
Federal Tax Liability - 2003	**$31,585**	**$43,361**	**$60,126**	**$121,869**	**$273,909**	**$478,458**
New York State - Old Law						
NYS Itemized Deductions - 2003	$28,633	$29,729	$30,762	$33,223	$46,018	$68,160
NYS Exemptions - 2003	$2,000	$2,000	$2,000	$2,000	$2,000	$2,000
NYS Taxable Income - 2003	$169,367	$218,271	$267,238	$464,777	$951,982	$1,592,840
NYS Tax Liability - 2003	**$11,602**	**$14,952**	**$18,306**	**$31,837**	**$65,211**	**$109,110**
New York State - New Law						
NYS Tax Liability with Rate Increase	**$12,703**	**$16,370**	**$20,043**	**$34,858**	$73,303	**$122,649**
Impact of NYS Tax Changes on Federal Taxes						
Federal Itemized Deductions with NYS Tax Changes	$40,795	$55,057	$59,497	$83,755	$153,919	$237,351
Federal Exemptions	$12,400	$8,680	$3,720	$0	$0	$0
Federal Taxable Income with NYS Tax Changes	$146,805	$186,263	$236,783	$416,245	$846,081	$1,425,649
Federal Tax Liability for 2003 with NYS Tax Changes	**$31,286**	**$42,912**	**$59,584**	**$120,892**	**$271,335**	**$474,184**
Combined Federal-State Impact of NYS Tax Changes						
NYS Tax Increase	$1,101	$1,419	$1,737	$3,021	$8,092	$13,539
Change in Federal Taxes due to Federal Tax Changes Since 2000 & H.R. 2	-$5,991	-$8,216	-$9,572	-$16,793	-$36,781	-$63,669
Change in Federal Taxes due to NYS Tax Changes	-$299	-$448	-$542	-$977	-$2,574	-$4,275
Net Change in Total Federal and State Income Taxes	**-$5,189**	**-$7,246**	**-$8,377**	**-$14,748**	**-$31,263**	**-$54,405**

The Effect on the Economy

- Because state and local income taxes paid are deductible from income in calculating federal income tax liability, the net impact on the affected taxpayers is much less than the revenue raised by the state. While property taxes are also deductible, the economic impact of deductibility of a high-end income tax increase is more significant since the affected taxpayers are much more likely to itemize their deductions and are in higher federal tax brackets (which increases the value of deductibility) than the broad range of real property tax payers. The result is that the federal government pays about a third of the bill.
- The approach adopted by the Legislature also has a much less negative effect on the New York economy than the alternatives proposed by the Governor (cuts in state and local services and/or increases in local property taxes) since over 15% of the personal income tax increase is being paid by residents of other states and other countries.
- As indicated above, the new 7.7% top rate is approximately half of what New York State's top personal income tax rate (15.375%) was in the early and mid-1970s. At that time, New York had the 3rd highest income tax rate of all the states with income taxes. The temporary 7.7% top rate places New York 15th among the 42 states with personal income taxes.
- It is also important to note that over the course of the last quarter century, as New York has substantially reduced its top personal income tax rates, the states with which it has the most direct economic competition, Connecticut and New Jersey, have moved in the opposite direction. New Jersey's top rate is now 6.37%, more than two and a half times higher than its mid-1970s rate and, since 1991, Connecticut has had a broad-based personal income tax, the top rate of which was recently increased from 4.5% to 5%.

Top State Personal Income Tax Rates on Earned Income

	1976	1985	2004
New York	15.375%	9.5%	7.7%
New Jersey	2.5%	3.5%	6.37%
Connecticut	0	0	5.0%

Note: Prior to 1991, Connecticut taxed the interest, dividends and capital gains of high income residents but it did not tax business income, wages, salaries, and other income. From 1978 through 1988, New York employed a dual rate system in which it applied a higher top rate to investment income than to wages, salaries, and business income. For 1985, the top rate applicable to investment income was 13.5%.

The Economic Impact of the 2003 Budget Agreement: The Example of the School Aid Restorations

- The 2003-04 Executive Budget proposed a $1.24 billion (8.5%) cut in school aid over the previous school year. This represented a cut of over $1.8 billion against the increase that would have been necessary to allow for school districts to maintain current services without increasing the portion of their budgets financed through local revenue sources - primarily the real property tax. The Legislature ended up restoring over $1 billion of this reduction, leaving a year-to-year cut of $207 million or 1.5%. The Legislative restorations had three important consequences:

  - <u>Educationally</u>, the restorations meant that school districts could maintain programs and services of importance to student achievement and avoid lay offs of teachers and other critical school staff.

  - <u>Fiscally</u>, local school districts were able to substantially reduce the magnitude of the real property tax increases which would have been necessary to avoid deep cuts in services without the additional state aid. The New York State Council of School Superintendents reviewed data from 518 school districts that amended their Property Tax Report Cards between the original and revised filing deadlines which occurred, respectively, before and after the Legislature voted to over-ride the Governor's budget vetoes. This study found that these districts, which received an additional $394 million in state aid as a result of the Legislature's restorations, responded in the following way:
    - 147 districts raised their proposed spending by a total of $38 million
    - 383 districts lowered their proposed tax levy by a total of $189 million

    This report also pointed out that "the proposed 2003-04 tax levy for all districts as of April 28th (before the Legislature passed its budget the first time) was $294 million less than what could have been expected given the Governor's proposed aid cuts and the spending increases they were seeking. This suggests that many districts were either budgeting for Legislative aid restorations, spending down reserves, or using some combination of strategies. And some still reduced their projected tax levy in amended Property Tax Report Cards."

- Economically, restoring the education cuts and paying for those restorations with a high-end income tax increase was a far better alternative than implementing the cuts as proposed. If the school aid cuts could have been restored without paying for them (which is an unrealistic alternative) the benefits would have been substantial.

  - An analysis of this unrealistic alternative, using the same input-output economic model used by the Empire State Development Corporation to evaluate economic development proposals, found that adding $1.84 billion in spending to the state education system without having to pay for this investment would generate about 79,000 jobs per year in each year 2004 through 2007 and increase Gross State Project by over $2.5 billion each year.

  - A fiscally responsible "balanced budget" alternative that increased state aid to education by $1.84 billion over the level proposed by the Governor and funded that increase in state aid with a concomitant and offsetting $1.84 billion increase in the state individual income tax would increase employment by about 56,000 jobs and Gross State Product by more than $1.5 billion a year. This analysis confirmed the theoretical arguments regarding the relative economic impact of spending cuts and tax increases on the state economy finding that even if taxes are increased to pay for a substantial increase in school spending that there will still be a net positive effect on the economy.

The Legislature's 2003 "budget choices" are supported by basic economic reasoning.

- Neither tax increases or service cuts are desirable during a recession. Both take demand out of the economy - making recessions longer and deeper, and making recovery more difficult.

- But New York, like most other states, is required to balance its budget in both good times and bad.

- So the states face a real dilemma during economic downturns - having to figure out what mix of spending cuts and tax increases will do the least harm. Ideally, during such periods, the federal government, which is not required to run balanced budgets and which is responsible in our governmental system for overall macroeconomic management, will assist the states with some form of counter-cyclical financial assistance.

- But what are the states to do during economic downturns absent federal aid or sufficient federal aid to avoid spending cuts and/or tax increases? Joseph Stiglitz, winner of the 2001 Nobel Prize in Economics, and Peter Orszag of the Brookings Institution, in their paper, ***Budget Cuts vs. Tax Increases at the State Level: Is One More Counter- Productive than the Other During a Recession?***, use basic economic reasoning to explain why a temporary increase in the tax on the portions of income over some relatively high level is the least damaging mechanism for balancing state budgets during recessions.   On the other hand, they conclude that basic economic reasoning indicates that reductions in government spending on goods and services that are produced locally (like education and healthcare) and reductions in transfer payments to lower-income families are most damaging to the economy since they come closest to taking dollar for dollar out of the local economy. Increases in consumption taxes and fees will take more demand out of the economy than tax increases on the portion of income over some relatively high level but less demand than cuts in locally-produced goods and services or transfer payments to lower-income families.

Closing the 2004-05 Budget Gap: The Governor's Approach

- This year's projected budget gap ($5.1 billion) is less than half the size of last years but in percentage terms the Governor is once again relying much more heavily on spending cuts ($2.6 billion according to the Executive Budget documents) than revenue increases ($972 million).
- The Executive Budget proposes to close the remainder of the gap ($1.5 billion) with nonrecurring actions or one-shots. The largest of the proposed one-shots are the shift of various pay-as-you go capital projects to bond financing ($283 million) and the use of $261 million of the projected 2003-04 surplus.
- On the revenue side, the two largest gap closing proposals involve eliminating the $110 clothing sales tax exemption and replacing it with four one-week exempt periods ($400 million) and reimposing an assessment on hospital and home-care revenues and increasing an existing reimbursable assessment on nursing homes. The Executive Budget estimates that the proposed health care assessments will generate $429 million during the upcoming fiscal year and $670 million per year on a full annual basis, with the amount of those revenues being used to help close the General Fund gap growing from $323 million in the upcoming year to $475 million in 2006-07.
- In addition to the increased health care provider assessments, the Executive Budget also reduces funding for health care on the expenditure side of the budget. While the direct Medicaid cuts proposed in this year's Executive Budget are not as great as in last year's and some could reduce costs without jeopardizing the quality of care, other of these cuts are particularly inconsistent with the Governor's rhetoric and with the actions of the Governor and the Legislature in recent years to reduce the number of New Yorkers without health insurance.

Executive Budget Proposals to Close the 2004-05 through 2006-07 Budget Gaps

($ Millions)

	SFY 2004-05	SFY 2005-06	SFY 2006-07
Projected Base Level Gap	$5,071	$6,727	$7,805
Total Spending Actions	$2,589	$2,495	$2,199
Medicaid/Health Care Cost Containment	$425	$539	$555
Pension Reform	$440	$301	$150
Restructure Welfare Programs/Maximize '	$362	$382	$396
Mental Hygiene Cost Containment	$298	$285	$214
Restructure TAP	$227	$268	$234
Restrain growth in building aid, BOCES, '	$186	$244	$268
Debt management	$150	$150	$174
NYC School Aid for SBE	-$70	-$100	-$100
Medicaid Long Term Care Takeover	-$24	-$132	-$258
All Other Spending	$595	$558	$566
Total Revenue Actions	**$972**	**$1,163**	**$1,118**
Sales Tax on Clothing	$400	$429	$451
Health Care Provider Assessment	$323	$475	$475
Criminal Justice Fees	$58	$113	$113
Quick Draw Enhancements	$43	$68	$68
Abandoned Property	$42	$3	
Fixed Dollar Minimum	$40	$40	$40
Pistol Permit Fee	$31	$11	$11
STAR Tax Credit	-$11	-$57	-$113
All Other Revenue	$46	$81	$73
Total Nonrecurring Actions	**$1,510**	**$219**	**$139**
Capital Projects Bond Financing	$283	$192	$139
Use of 2004-2004 Surplus	$261		
Delay of Medicaid Cycle	$190	-$190	
Additional Tobacco Benefit	$181		
LGAC Payment Restructuring	$170		
Federal Welfare Funds	$115		
Reverse Meyers Tax Decision	$50		
Use Available HFA Reserves		$225	
All Other	$260	-$8	
Remaining Gap	**$0**	**$2,850**	**$4,349**

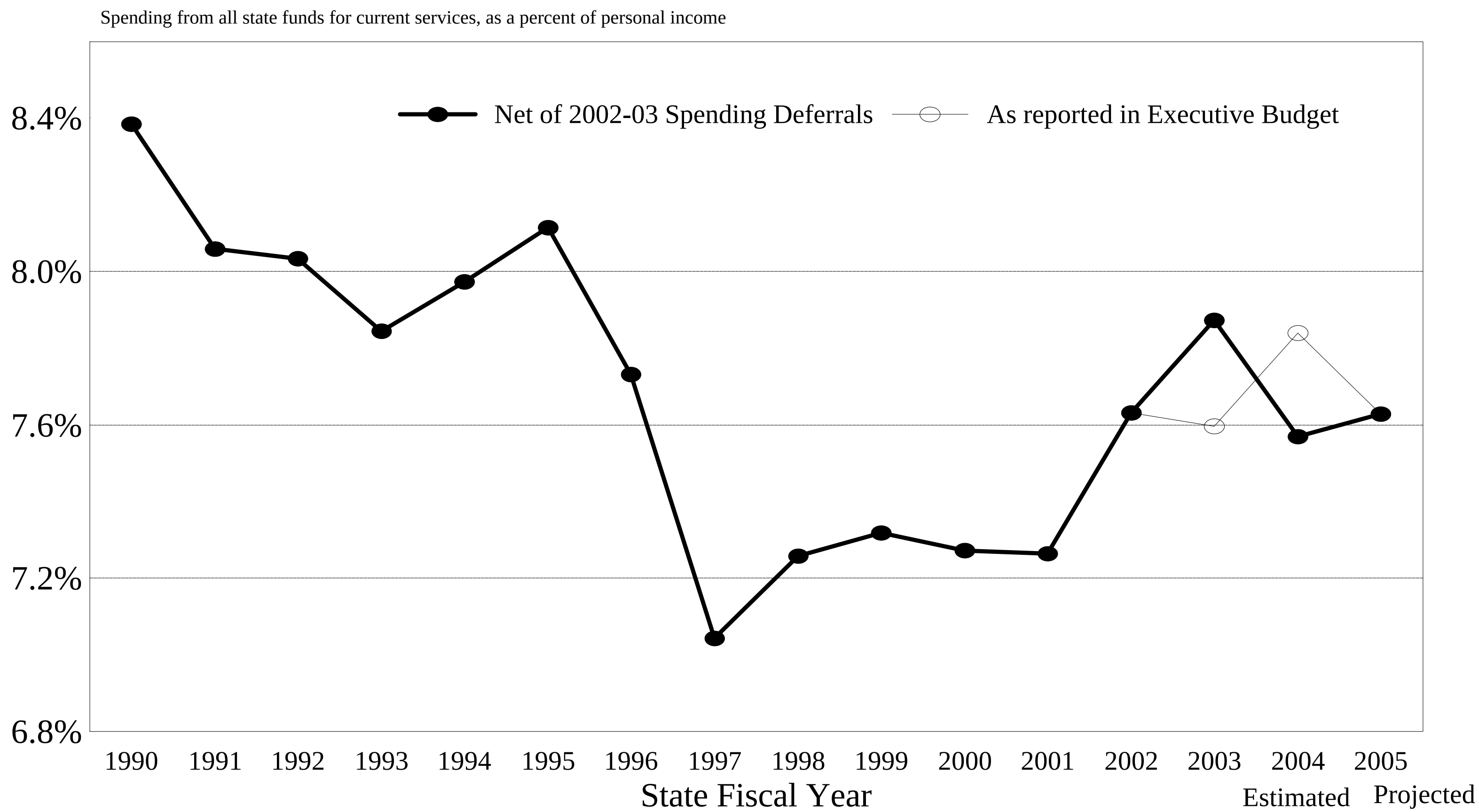
- In education, the Executive Budget proposes a freeze on operating aid to school districts and cuts or freezes in a number of aid programs under which school districts are reimbursed for a portion of their actual costs. In the latter category, the Executive Budget estimates that the proposed changes in building aid, transportation aid and BOCES aid would generate savings for the state (and, thus reductions in aid to school districts) of $186 million in the upcoming fiscal year growing to $268 million in 2006-07. Unlike in previous years, however, no estimate is given as to the savings to the state (or the losses to school districts) from the freezing of operating aid.
- The expenditure side gap closing actions also include 5% cuts in many other local aid programs (which together with a catch-all "efficiency in State agency operations" is estimated to save $595 million), a proposal to withhold one-third of college students TAP awards until "timely degree completion" ($227 million), and a cap on the annual increases in employer contributions to the state retirement system ($440 million). The two latter proposals are both long shots. The TAP withholding proposal has been advanced by the Administration before but it has always been rejected as illogical and as having a negative effect on the neediest of students. The pension contribution proposal is similar to a proposal advanced by the Administration last year but it is seen as unconstitutional by the State Comptroller, the sole trustee of the retirement system.
- The proposed freeze in state operating aid for school districts and cuts in other state aid programs will hurt the economy in several ways. Cuts in the quality of local educational programs and other local services will hurt communities' attractiveness to residents and employers and negatively impact school districts' ability to achieve higher performance standards. In addition, such cuts would reduce employment both directly and indirectly. On the other hand, to the extent that localities do not want to cut their educational or other programs, they will have to increase local property taxes more than would otherwise be necessary. Similarly many of the Governor's proposed savings in Medicaid and welfare costs will hurt people while also hurting local economies.

Impact of 2002-03 General Fund Payment Deferrals on Year-to-Year Changes in General Fund Spending

(amounts in millions of dollars)

	2002-03	**2003-04**	**2004-05**
General Fund spending as Shown in Executive Budget Financial Plans	$37,963	$42,160	$41,885
Adjustment for 2002-03 payments made in 2003-04	+$1,900	-$1,900	
General Fund spending net of 2002-03 payment deferrals	$39,863	$40,260	$41,885

Current services spending relative to the size of the economy has declined substantially since 1990.



Since 1990, New York State's expenditures for employee wages and salaries have declined in real terms by over $750 million, or almost 7%.

Personal Service expenditures in millions of SFY 2003 dollars

	General Fund	Special Revenue Funds	Total
State FY 1989-90	$6,907.5	$3,949.2	$10,856.6
State FY 1994-95	$5,543.0	$4,627.0	$10,170.0
State FY 2002-03	$5,694.0	$4,408.8	$10,102.8
Average Annual Change			
1989-90 to 1994-95	-$272.9	$135.6	-$137.3
1994-95 to 2002-03	$30.2	-$43.6	-$13.4
Average Annual Percent Change			
1989-90 to 1994-95	-4.31%	3.22%	-1.30%
1994-95 to 2002-03	0.54%	-0.96%	-0.13%
Total 13 -Year Change			
Amount	-$1,213.5	$459.6	-$753.8
Percent	-17.57%	11.64%	-6.94%

The 2004-2005 Executive Budget Proposal virtually freezes school aid and if adopted would lead to double digit property tax increases in the poorest districts or the loss of programs and services to the neediest students or both.

- The Executive Budget proposes to merge six existing operating aid programs and cost reimbursement aid for public special education placements into a single block grant, which the Governor calls Flex Aid, with no increase in funding from last year. Three other grant programs (Prekindergarten, Class Size Reduction and Minor Maintenance) would be frozen at this year's funding level. While aid for private special education placements would be frozen at the statewide level, individual districts would see less aid if their costs for such purposes increased less than other districts. While districts transportation aid (a cost reimbursement program) could increase, those increases for transportation operations would be capped at 2.5%. And for BOCES aid, another cost reimbursement program, school districts would be entitled to receive only the lesser of their prior year's aid or what they would otherwise be eligible to receive for the current year. Building aid would be limited to projects for which districts notified the State Education Department of a signed construction contract prior to November 15, 2003. Taken together, these Executive Budget proposals would increase aid by about 1% for the 2004-2005 school year with that increase being for a **reduced** state contribution to cost reimbursement programs.
- The New York State Educational Conference Board has estimated that, on average, school districts must spend about 5% more in 2004-2005 than in 2003-04 to simply maintain current programs and services given the scheduled increases in health insurance premiums, pension contributions, salaries and other components of school budgets. Contributions to the Teachers Retirement System, for example, are scheduled to at least double, from 2.52% of payroll this year to between 5% and 6% next year, and most health insurance premiums are currently increasing by more than 10% per year. Applying these growth rates, the Conference Board concluded that school districts statewide would have to spend $1.3 billion more in school year 2004-2005 just to maintain the current level of services. To avoid shifting an increasing share

of these school costs onto the local property tax base, the state would have to provide an increase in aid of between $600 and $650 million - a far cry from the $150 million increase proposed in the Executive Budget.

C And, as the following table demonstrates, a freeze in operating aid such as that being proposed this year by the Governor, hurts poorer districts much more than wealthier districts. Since state aid comprises a much larger share of the budget of needier districts than of wealthier districts, a freeze (or a low percentage increase) in state aid will place much greater pressure on the budgets of needier districts.

Impact of Executive Budget Proposal on Local Property Tax Rates

	2003-2004	2004-2005	Percent Increase
Wealthy School District			
School Aid (millions)	$2.0	$2.0	**0 %**
Property Tax (millions)	$8.0	$8.5	**6.25%**
Total Budget (millions)	$10.0	$10.5	**5 %**
Poor School District			
School Aid (millions)	$8.0	$8.0	**0 %**
Property Tax (millions)	$2.0	$2.5	**25%**
Total Budget (millions)	$10.0	$10.5	**5 %**

The CFE Decision and the Governor's Proposed School Spending Cap

C The New York State Court of Appeals, in its decision in the Campaign for Fiscal Equity, concluded that money, and the educational inputs that money buys, clearly matters - if it is used effectively. The Court's order in this decision links these issues together in an interesting and effective manner:

> "Reforms to the current system of financing school funding and managing schools should address the shortcomings of the current system by ensuring, as a part of that process, that every school in New York City would have the resources necessary for providing the opportunity for a sound basic education. Finally, the new scheme should ensure a system of accountability to measure whether the reforms actually provide the opportunity for a sound basic education.
>
> "The process of determining the actual cost of providing a sound basic education in New York City and enacting appropriate reforms naturally cannot be completed overnight, and we therefore recognize that defendants should have until July 30, 2004 to implement the necessary measures."

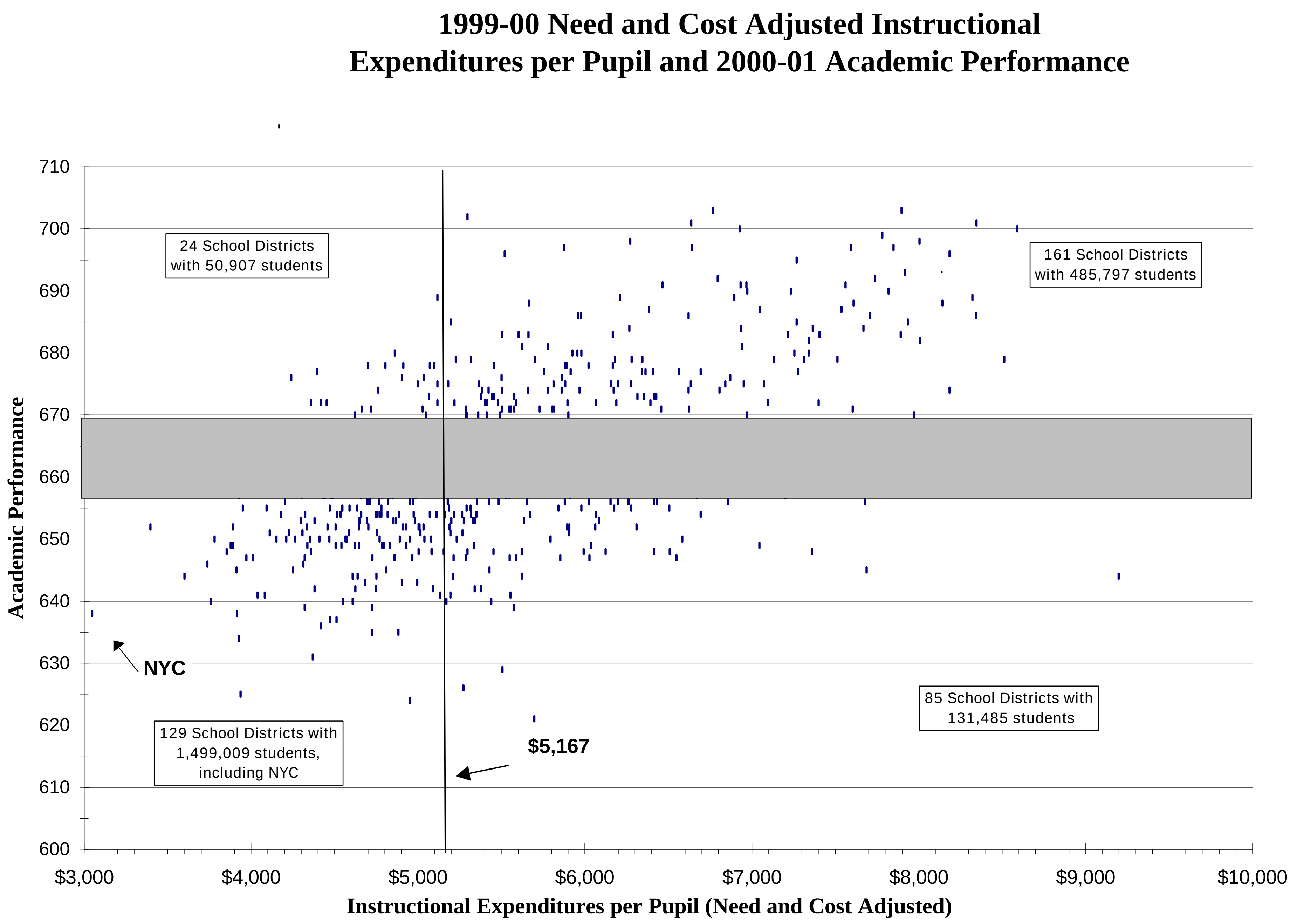
C While the ruling in this decision applies only to New York City, education advocates are generally hopeful that New York State will develop and implement a statewide solution that ensures that all school districts in the state have the resources necessary to provide all of the state's children with a sound basic education. In proposing "a new and separate dedicated fund to help meet the cost of a sound basic education." Governor Pataki seemed to endorse a statewide approach when he indicated that the resources in this fund would be "dedicated to New York City and other high needs districts." Whether a dedicated fund is an appropriate approach, and whether the revenue source (Video Lottery Terminals) recommended by the Governor for this fund is appropriate and adequate for the job involved, requires a full and thorough debate. But the Governor's focus on "ensur(ing) that every child has the opportunity to receive the best possible education" makes an important contribution to that debate.

- So what does this mean in terms of school district needs and resources? Research by the State Education Department has indicated, the costs of the educational programs needed to provide all students in high-needs school districts is much greater than the statewide average. As the accompanying scatter plot indicates, as spending per pupil increases, with those calculations weighted to reflect the greater needs of pupils living in poverty, median test scores rise.

- While the Campaign for Fiscal Equity is still in the process of identifying the cost of a sound basic education in different parts of the state and in different types of school districts, it is clear that any plan to ensure a sound basic education with the needed accountability measures will involve what school finance specialists refer to as leveling up spending in high needs districts. And since many of these high needs districts are also districts with relatively low resources, substantial increases in state aid will undoubtedly be necessary.

- In this context, the Governor's proposed spending cap (which would cap year-to-year increases in school budgets at the lesser of 4% or 120% of the increase in the Consumer Price Index,[3] unless a district sought and received a 2/3rds majority vote in a school budget referendum) is illogical for several reasons. First, as a percentage increase cap, this proposal would institutionalize and exacerbate whatever inequities are present in the current system. Second, the legislation proposed by the Governor would exempt from this cap "expenditures required due to a judgment that has been entered by a court that such district does not provide a sound basic education." Hopefully, school districts will be provided with the resources necessary to fund a sound basic education without the need for district-by-district court orders. Third, the Governor has proposed to give taxpayers in districts that comply with this cap a state income tax credit equal to a percentage of their STAR property tax exemptions. The benefits under STAR are already inequitably distributed and such a credit would increase these inequities.

[3] For the 2004-05 school year, under the Governor's proposal, school budget increases would be capped at 2.28% unless the required 2/3rds vote was received.


1999-00 Need and Cost Adjusted Instructional
Expenditures per Pupil and 2000-01 Academic Performance
24 School Districts
with 50,907 students
161 School Districts
with 485,797 students
129 School Districts with
1,499,009 students,
including NYC
85 School Districts with
131,485 students
NYC
$5,167
Academic Performance
710
700
690
680
670
660
650
640
630
620
610
600
$3,000
$4,000
$5,000
$6,000
$7,000
$8,000
$9,000
$10,000
Instructional Expenditures per Pupil (Need and Cost Adjusted)

The Governor's 2004-2005 budget proposal includes a number of proposals which will make it much harder for needy families to make ends meet.

- **Grant Reductions for Families with Disabled Members:** Modification of the grant eligibility determination methodology for households which include a SSI recipient would save the state approximately $10 million per year but reduce benefits to about 26,700 families by an average of $90 per month. The Office of Temporary and Disability Assistance (OTDA) has already submitted proposed regulations to implement these changes.

- **Changes to the Earned Income Disregard:** The budget proposes to limit the Earned Income Disregard to 50% (it is currently 51% and indexed to changes in the federal poverty guidelines) for recipients on welfare less than two years; reduce the disregard percentage to 25% for recipients on welfare more than two years but less than five years and eliminate the disregard entirely for recipients on welfare more than five years.

- **Benefit Cuts for Long Term Recipients:** Families on assistance for five years and individuals and childless couples on assistance for more than one year would face a 10 percent reduction in the non-shelter portion of their public assistance grant.

- **Full Family Sanctions:** Currently public assistance benefits are withheld only from the head of household for noncompliance with work requirements. The Executive Budget proposes the elimination of public assistance benefits to the entire household if the head of household does not comply with work requirements.

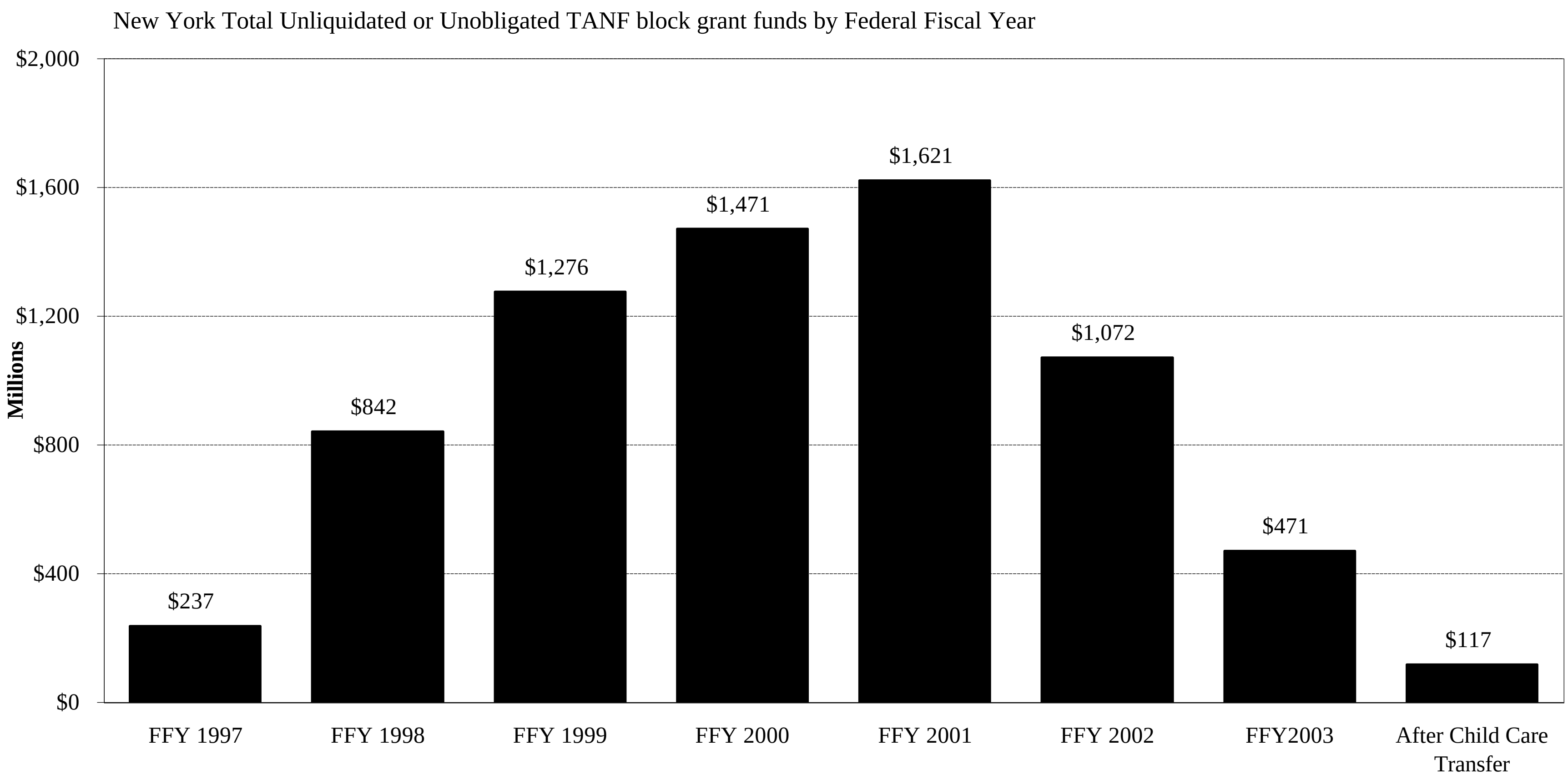
- According the to the Executive Budget, these proposals together will close about $88 million of the $5 billion budget gap. While providing no more than a minuscule contribution to the current fiscal crisis, they impose considerable hardship on public assistance families. For example, the change in benefit calculation for families including an SSI recipient will reduce monthly public assistance benefits for some families by more than 10%. The elimination of the Earned Income Disregard for families after five years of assistance could reduce the income of a family with a full time, year round worker earning the minimum wage by as much as 15%.

- These proposals also introduce perverse incentives to New York's public assistance system by penalizing families who are doing the "right" thing — working long hard hours — merely because they are stuck in low paying jobs that do not enable them to earn enough to support their families without public help.

- These proposals also fly in the face of what basic economic theory tells us is needed in a recession. They take money away from the families with the highest marginal propensity to consume and therefore would have a very negative impact on the state's economy.

- Full family sanctions will punish children for the actions or inactions of their parents despite the fact that research has found that states with full family sanctions have not been any more successful in moving families from welfare to work than states (California and New York) which do not currently exercise this option. Sanctionable offenses can be as minor as being late for an appointment or not filing paperwork with the right office.

New York has just about depleted its TANF reserves. When the 2003-2004 Child Care Block Grant funds are transferred, New York's balance will be almost zero.



Source: ACF-196 submitted by New York State to the Department of Health and Human Services Administration for Children and Families

Use of the federal Temporary Assistance for Needy Families (TANF) block grant to plug budget wholes has exhausted New York's federal reserves and severely reduced the resources available for programmatic initiatives.

- C One budget balancing strategy used last year was to delay the transfer of the fund to the Child Care Block Grant until after the federal fiscal year that ended September 30, 2003. When those $300+ million in resources are transferred, New York will have exhausted the reserves accumulated in the six years of the program's existence.

- C One factor contributing to the current year's $5 billion gap is the fact that there are no longer sufficient TANF funds to continue to fund TAP and other non-welfare programs with TANF resources. Even funding for the Title XX block grant which supports critical child welfare services has been reduced due to the depletion of TANF funds.

- C Once again the Governor is proposing significant cuts in the programs and services designed to help families transition for welfare to work. The Governor's budget calls for the elimination of funding for $43 million in "legislative initiatives" and once again proposed a reduction in funding for summer youth employment. Most other "TANF surplus" programs are cut by 10%.

New York should be helping its low-income families work towards self-sufficiency by increasing the minimum wage, maintaining and strengthening work incentives and investing in services and programs to help families move from welfare to the labor force.

- New York should increase its minimum wage immediately to $7.00 per hour and prevent future erosion in its purchasing power by providing for automatic adjustments tied to the Consumer Price Index or Average Weekly Wages. This is a policy proposal that would encourage and reward work while helping to close the state's budget gap.

- New York should maintain and expand the current work incentives, particularly the Earned Income Disregard. Currently recipients are ineligible for public assistance when their total monthly income exceeds the <u>lower</u> of the poverty level or 185% of the standard of need. New York should change its eligibility rules to permit benefits until income reaches the higher limit to recognize the increased costs faced by families in those counties where 185% of the standard of need exceeds the poverty threshold.

- New York should invest in programs and services that help public assistance recipients gain skills and work experience which will help them earn high enough wages to no longer need public income support.

- New York should devote more resources to programs and services that remove barriers that prevent public assistance recipients from moving into the work force rather than focusing on mean spirited reductions in already extremely low benefits or punitive sanctions to try to "push" recipients off the welfare rolls.

Increasing the minimum wage would save the state as much money as eliminating the earned income disregard and would increase rather than decrease family incomes.

Single Parent with Two Children, Albany County, Working Full Time, Full Year at the Minimum Wage

	With Current Earned Income Disregard	With Proposed Earned Income Disregard	With Current Disregard but Higher Minimum Wage
Minimum Wage	$5.15	$5.15	$7.00
Monthly Earnings	$824	$824	$1,120
Standard of Need	$510	$510	$510
Public Assistance Grant	$150	$0.00	$0
TOTAL MONTHLY INCOME	$974	$824	$1,120
Change in monthly income for family			
Dollar amount		-$150	$146
Percent change		-15%	15%
Change in governmental expenditures		-$150	-$150

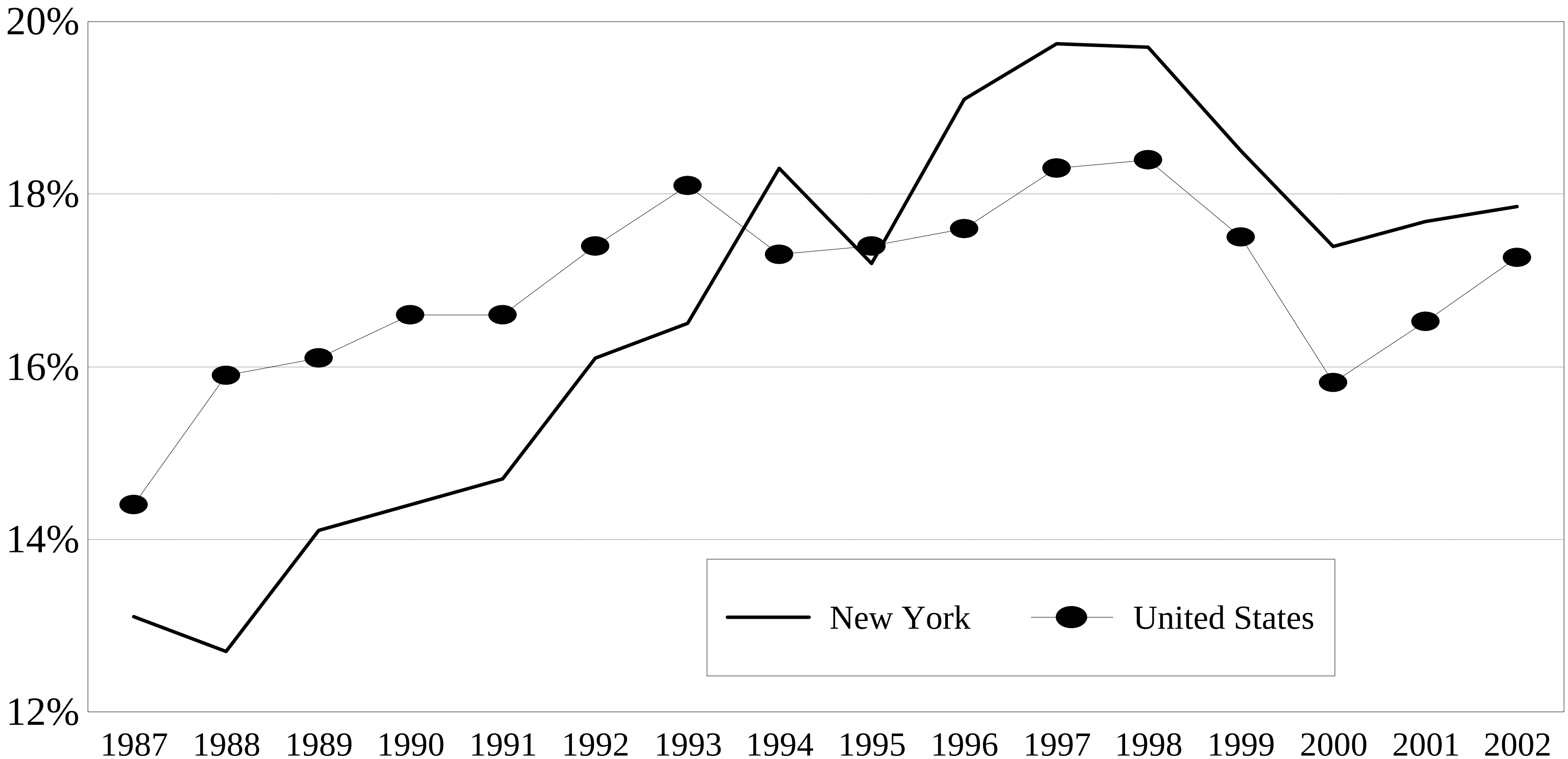
Many of the Governor's health care proposals are inconsistent with his rhetoric and with common sense.

While on the one hand the Governor speaks with pride of our health care system as "the best in the nation," the Executive Budget proposes numerous benefit and eligibility changes which would seriously weaken our health care "safety net."

- In his budget address, Governor Pataki indicated that "his budget includes an historic and sweeping set of Medicaid reforms and cost-saving measures that will improve the quality of service." In reality, however, the Executive Budget would eliminate Medicaid coverage for so-called "optional" services -- podiatry, dentistry, audiologists and psychologists — hardly "improvements in the quality of service." The Governor's budget also eliminates dental and vision services for Family Health Plus participants..

- While the Governor notes that "through programs like child Health Plus, Healthy New York, EPIC and Family Health Plus we are providing quality health care to hundreds or thousands of children, seniors and low income workers," his budget proposes to
  - Reduce facilitated enrollment for Child Health Plus and eliminate facilitated enrollment for Family Health Plus
  - Increase copays for services and prescription drugs
  - Impose the Medicaid asset/resource test on applicants for Family Health Plus
  - Require a 12-month waiting period for Family Health Plus applicants who had group health insurance previously
  - Prohibit coverage under Family Health Plus for individuals employed by a large business or government entity
  - Transfer children ages 6-19 with incomes between 100% and 133% of the Federal Poverty Line from Medicaid to Child Health Plus

As the Governor proposes cuts in Medicaid and more stringent eligibility guidelines for Family Health Plus, 3 million New York adults still lack health insurance.



The Pros and Cons of the Governor's Proposal for a State Takeover of the Costs of Long Term Care.

Assuming that adequate revenue sources are in place, so as to ensure that other important state services are not jeopardized, a state takeover of a greater portion of the local share of Medicaid costs is a good idea for the following reasons.

- Since state revenue sources are generally more progressive than those currently authorized to local governments in New York State, such a change has the potential for making New York State's overall state-local tax system more progressive.
- Such a change has the potential for reducing fiscal disparities within the state. Fiscal disparities arise because tax capacity is not distributed among counties in the same manner as low income individuals in need of medical assistance.

At the same time however, the Governor's proposal raises the following red flags:

- Taking all of over the local share of long term care costs rather than a greater portion of overall Medicaid costs in implicitly unfair to New York City. In New York City long term care expenditures represent only about 50% of all Medicaid expenditures while for the rest of the state, because of its lower poverty rates, long term care expenditures represent about 75% of all expenditures.
- If the State took over 100% of this category of Medicaid but left counties with 50% of the nonfederal share of other categories, counties would have little incentive to ensure that only eligible individuals were able to access Medicaid for long term care and on the flip side, would have a disincentive to ensure that all eligible children and families were enrolled in the Medicaid program.[1]

If the state concludes that it is fiscally possible to increase the state share of Medicaid costs by a given amount of money, it could use that amount in a way that avoids these two problems.

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[1] One other alternative that has been discussed that also suffers from this same problem is the proposal to simply cap the dollar amount of the local contribution to Medicaid at current levels.

Closing the 2004-05 Budget Gap: Alternative Approaches

Many of the cuts and freezes proposed in the Executive Budget would have negative effects on the state's economy and its quality of life. In order to balance the 2004-05 budget in a more economically sensible manner, the following approaches should be considered:

- **Federal Assistance.** New York's government, labor and business leaders should work with their counterparts in other states and at the national level to secure an extension of the temporary "state fiscal relief" package enacted in May 2003 and the implementation of other steps necessary to protect state finances and provide appropriate federal assistance.
- **Public Procurement Reform.** Reduce wasteful contracting out to high priced consultants. Use the state's purchasing power to get better prices on prescription drugs.
- **Corporate Tax Reform.** New York State should even the economic playing field by eliminating corporate tax avoidance schemes and instituting appropriate corporate tax reforms so that all corporations pay a fair share of taxes and that government subsidies are only provided for jobs actually created.
- **Sales Tax Reform.** Continue the efforts begun last year to implement the Streamlined Sales Tax Project so that New York retailers do not face unfair competition from remote sellers. More aggressively enforce current laws on the collection of sales and use tax by remote sellers. Consider the extension of the sales tax base to include additional services.
- **Environmental Tax and Fee Reform.** Expand the bottle bill to a broader range of beverages, raise the deposit to 10 cents, and reclaim a portion of unclaimed deposit revenues for public purposes. Ensure that the tradable emission permits under Governor Pataki's proposed regional carbon cap proposal are auctioned rather than given away in order to ensure that the windfall revenues to be generated are available to mitigate the proposals negative effects and to serve other economically and socially important purposes. Consider expanding on the types of environmental charges proposed in this year's Executive Budget.

Closing the 2004-05 Budget Gap: Federal Assistance

New York's government, labor and business leaders should work with their counterparts in other states and at the national level to secure an extension of the temporary "state fiscal relief" package enacted in May 2003 and the implementation of other steps necessary to protect state finances and provide appropriate federal assistance.

- New York leaders should work for the extension of **the temporary federal revenue sharing program and the temporary increase in Medicaid match rates that were enacted into law in May 2003**. These programs are currently providing $20 billion in assistance to State and local governments including $2.1 billion for New York. Approximately $1.4 billion of this total is being used by the State government to help close its SFY 2003-04 and SFY 2004-05 budget gaps. Additional federal assistance, of a comparable amount, is necessary if the states are to avoid counter-productive budget balancing actions during their 2004-05 and 2005-06 fiscal years.
- New York leaders should attempt to build regional and national coalitions in support of **HR5523/S3055 which would repeal the limit that the Congress enacted in 2000 on the size of the loans that the federal government can make to state and local governments for tax revenue losses directly attributable to presidentially-declared major disasters**. This legislation would also waive the requirement for the repayment of such loans when the losses involved are the result of terrorist attacks. This could provide both New York State and New York City with at least $1.6 billion in aid to make up for September 11-related tax revenue losses.
- New York's public and private sector leaders should urge Congress to enact a version of **the American Parity Act.** This measure would provide funding for the rebuilding of US schools, hospitals and other infrastructure in an amount equal to the similar infrastructure amendments that we are making in Iraq. The funding for such an investment program could be provided by repealing the portions of the recently enacted tax cuts that benefit only the wealthiest Americans. This would trigger nearly $23 billion in investment in State infrastructure and could generate at least $2 billion for NY.

Closing the 2004-05 Budget Gap: Public Procurement Reform

C **Reduce Wasteful Contracting Out By the New York State government.** The Public Employees Federation has documented that up to $250 million is wasted by NYS each year by contracting out work that could be done by State employees at a significantly lower cost. There are numerous State contracts under which NYS pays contractors up to four times the salary of a State employee (including a 35% fringe benefit factor) to do the same work done by State employees. A more rational approach to contracting out would protect state taxpayers by requiring a cost/benefit analysis before a contract for personal services is executed to determine whether those services could be performed at a lower cost by State employees. Maine and Massachusetts have already adopted legislation restricting wasteful contracting out. The current system could also be improved through disclosure with each agency's proposed budget of information regarding proposed state operations personal service contracts.

C **Spend Less on Prescription Drugs by Combining State and Local Purchasing Power to Get Lower Prices.** The savings of aggressive action on this front are substantial. For example, the Health Reform Program at Boston University School of Public Health has estimated (using data for 2000) that New York could reduce its Medicaid expenditures by over $400 million per year if it were able to purchase brand name prescription drugs at federal supply schedule prices. These researchers have also concluded New Yorkers would have saved $3 billion in 2001 if international pharmaceutical makers accepted the same prices for brand name prescription drugs in the United States that they charge in Canada. The State's share of these savings would easily exceed $1 billion.

Closing the 2004-05 Budget Gap: Corporate Tax Reform

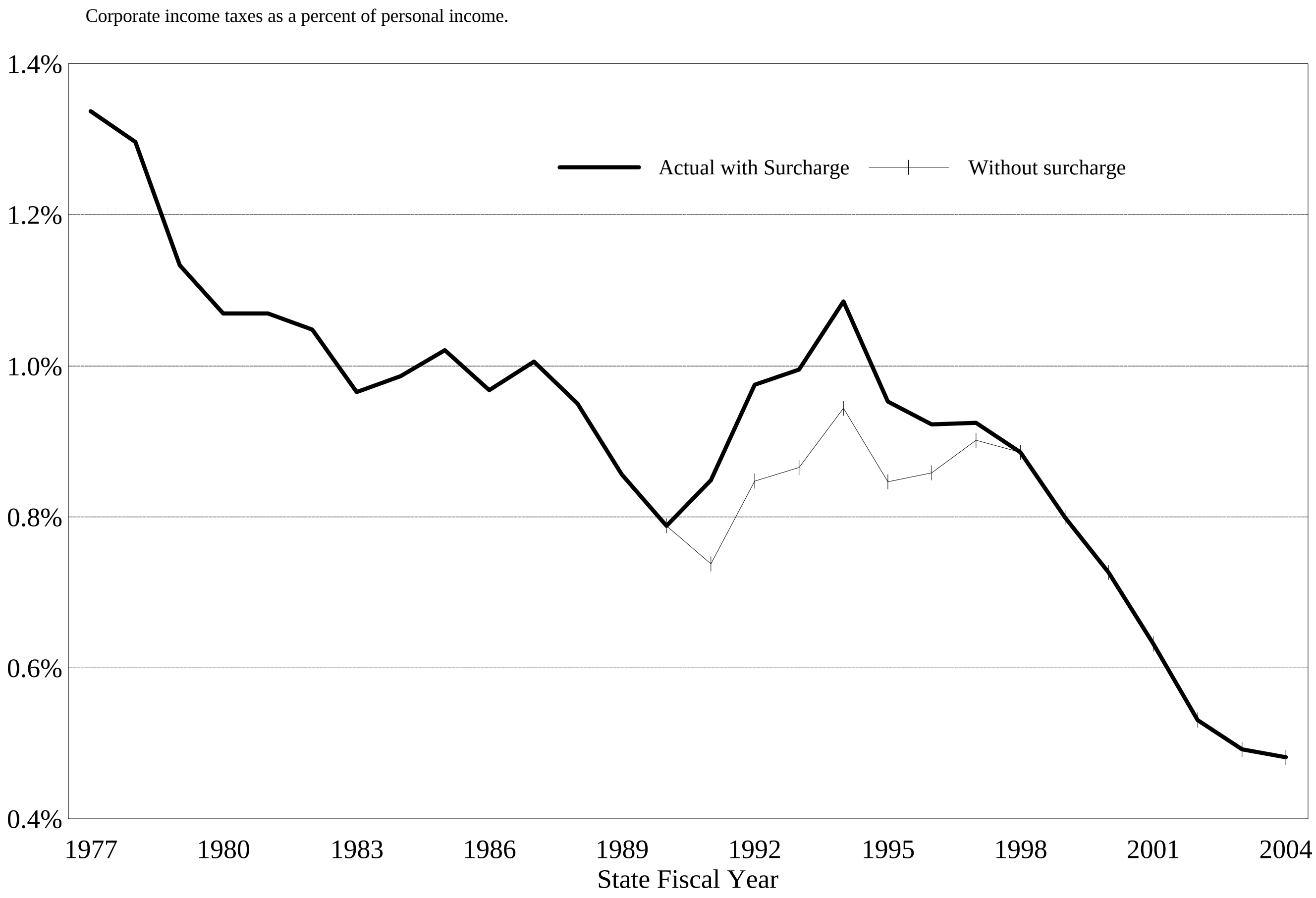
- **Eliminating specific loopholes that do not create jobs** could raise between $200 to $250 million annually and an additional $250 million in SFY2004-05 and SFY2005-06. Such actions include reform of the Empire Zone program ($50 to $100 million annually), reducing the abuse of "point-of-service" exceptions ($75 million), limiting Industrial Development Agencies' ability to abate State taxes ($60 million), and recovering subsidies from companies that do not live up to the conditions of their tax abatements ($15 million).

- **Reform New York's Corporate Alternate Minimum Tax (AMT).** Several significant loopholes were added to New York's Corporate AMT in 1994. These changes could be repealed. Alternatively, New York's current AMT could be replaced with a variation of the Alternative Minimum Assessment (AMA) adopted by New Jersey in 2002. While the New Jersey AMA applies to all businesses with gross profits of $1 million or more, New York could apply such an assessment only to businesses with gross profits of over $5 million in order to ensure that this revision would not hurt small businesses.

- **Crack down on schemes that create "Nowhere Income."** Many large corporations pay no taxes on profits derived from sales made in states in which they do not have a physical presence. 25 states, including Texas, Utah, Oregon and California, have enacted "throwback rules" to ensure that profits earned in a state in which a corporation may not be subjected to an income tax are taxed instead by its home state.

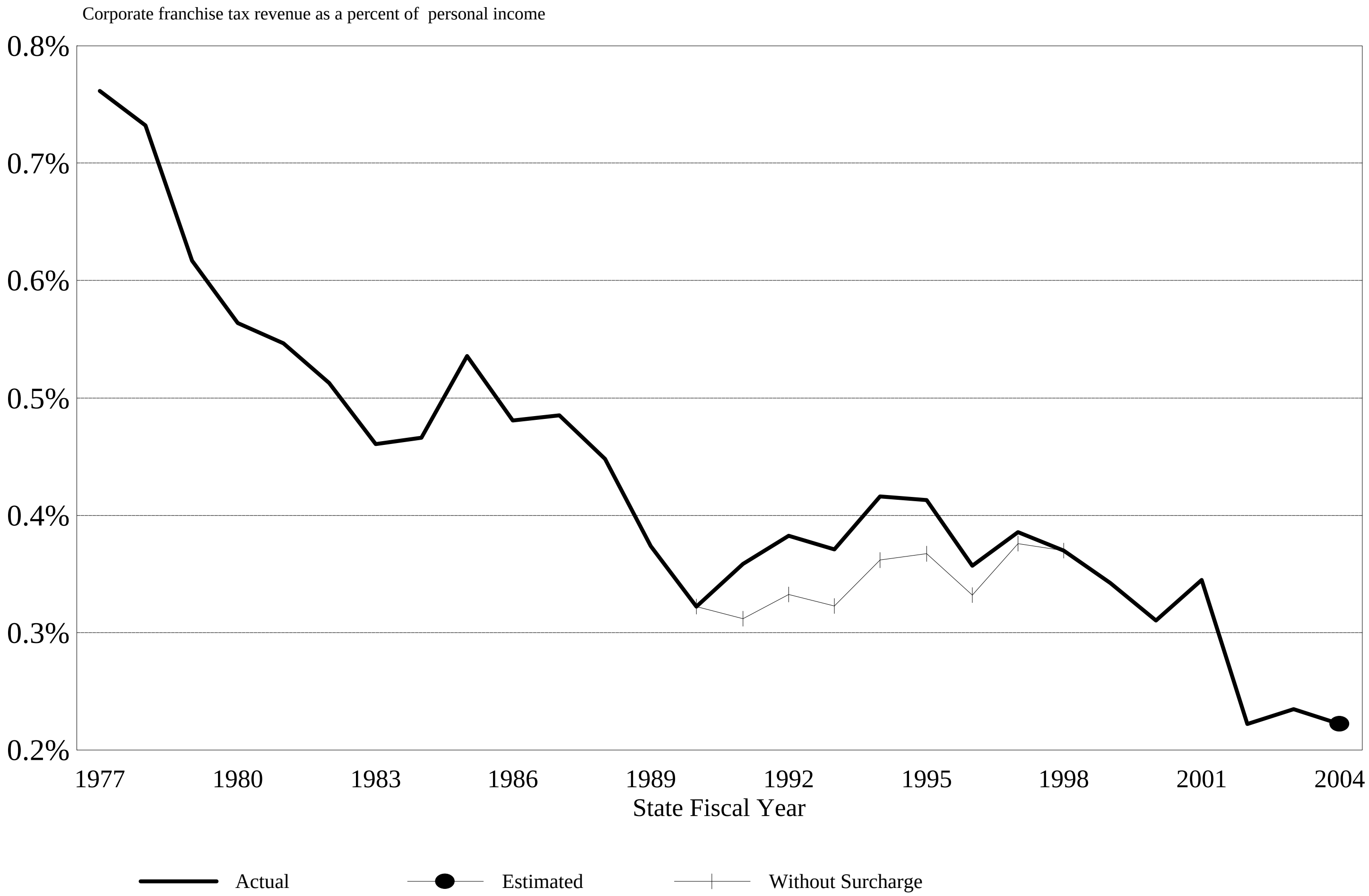
- **Adopt "Combined Reporting."** 16 states including California, Colorado, Illinois, and New Hampshire require multi-state and multi-national corporations to file a combined return for their entire "corporate family" rather than being able to use inter-subsidiary transactions to move income to countries or states where that income is not taxable. Under combined reporting, a corporate family files a single tax return covering the income of all of its subsidiaries, with that income apportioned among the states based on the locations of all its property, payroll and sales.

Corporate income tax revenues have fallen substantially relative to the size of the economy.



Note: Includes the state's main income tax on general coroporations (the Corporate Franchise Tax, Article 9-A & 13), as well as the Corporation and Utilities Tax (Article 9), the Insurance Tax (Article 33) and the Bank Tax (Article 32).

For example, revenues from the state's main tax on general business corporations has fallen by over 50% relative to the size of the state's economy.



Note: The increase in corporate tax revenues from SFY 1999-00 to SFY 2000-01 is due primarily to the impact of legislation which moved energy companies to the corporate franchise tax.

Economic Backdrop

and

Economic Policy Issues

The recession hit New York harder than the nation. Despite some job growth in 2003, December 2003 job levels are still well below levels when the recession officially ended.

Employment (in thousands)	New York	US
March 2001	8,669	132,527
November 2001	8,481	130,900
December 2003	8,405	130,124
March 2001 - November 2001 (Recession)		
Absolute Change	-189	-1,627
% Change	-2.2%	-1.2%
November 2001 - December 2003 ("Recovery")		
Absolute Change	-76	-776
% Change	-0.9%	-0.6%
March 2001 - December 2003		
Absolute Change	-264	-2,403
% Change	-3.0%	-1.8%

Source: Bureau of Labor Statistics (BLS).

In addition to New York City, many upstate areas had steep job losses from the First Half of 2001 to the First Half of 2003

	Employment		Change	
	1st Half 2001	1st Half 2003	#	%
New York State	8,615,050	8,357,817	-257,233	-3.0%
10 County Downstate Area	5,483,950	5,275,100	208,850	-3.8%
New York City	3,718,483	3,517,567	-200,917	-5.4%
Nassau-Suffolk	1,213,600	1,207,000	-6,600	-0.5%
Westchester County	417,800	414,550	-3,250	-0.8%
Rockland County	110,583	111,867	1,283	1.2%
Putnam County	23,483	24,117	633	2.7%
Upstate	3,145,150	3,088,700	-56,450	-1.8%
Upstate Metropolitan Areas	2,571,300	2,517,783	-53,517	-2.1%
Albany-Schenectady-Troy	460,450	457,683	-2,767	-0.6%
Binghamton	119,983	113,067	-6,917	-5.8%
Buffalo-Niagra Falls	551,783	542,650	-9,133	-1.7%
Dutchess County	118,667	119,600	933	0.8%
Elmira	43,450	40,800	-2,650	-6.1%
Glens Falls	50,467	50,100	-367	-0.7%
Jamestown	58,633	56,850	-1,783	-3.0%
Newburgh	132,250	133,400	1,150	0.9%
Rochester	551,000	524,350	-26,650	-4.8%
Syracuse	350,317	346,767	-3,550	-1.0%
Utica-Rome	134,300	132,517	-1,783	-1.3%
Non-metropolitan areas	573,850	570,917	-2,933	-0.5%

Note: Since the statewide total is estimated separately from the substate components in the monthly employment survey, the components may not sum to the state total.

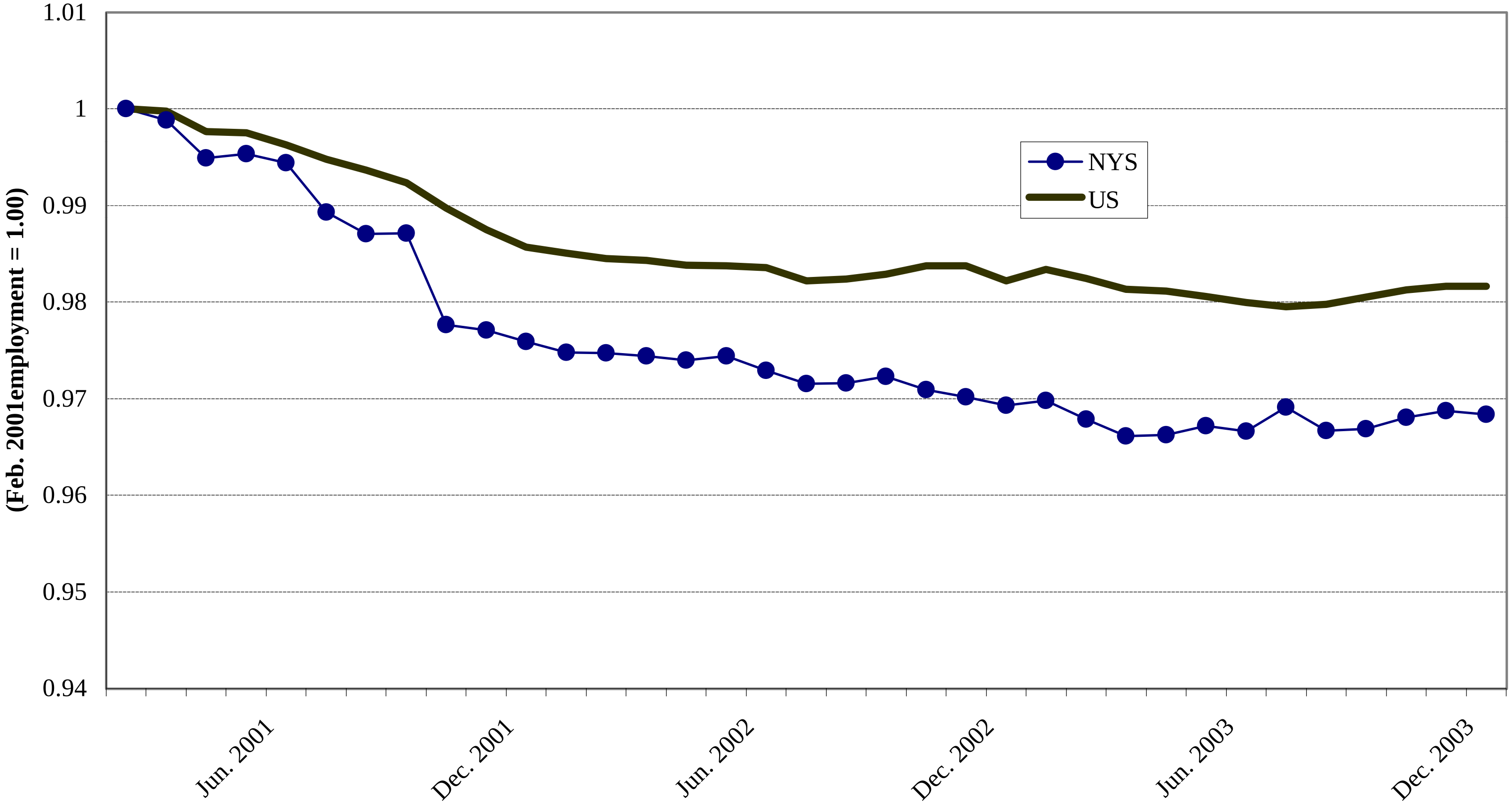
Source: 790 monthly payroll survey. NYS Department of Labor

Most of New York's job loss from March 2001 to March 2003 occurred in industries paying at or above the average for all industries.

March 2001 to March 2003	Average annual wage, NYS (2002)	New York (in thousands) March 01	March 03	Change	% Change	US % Change
Financial activities	$103,744	742	694	-48	-6.5%	1.8%
Information	$66,569	330	281	-49	-14.9%	-11.2%
Professional and business services	$58,626	1,108	1,023	-85	-7.6%	-4.7%
Wholesale trade	$55,941	371	353	-18	-4.9%	-4.0%
Construction	$47,721	306	295	-12	-3.8%	-2.2%
All Industries	**$46,328**	**8,603**	**8,323**	**-279**	**-3.2%**	**-1.8%**
Manufacturing	$46,299	728	621	-107	-14.7%	-12.2%
Transportation and utilities	$43,390	283	263	-20	-7.2%	-6.0%
Public administration	$42,947	1,479	1,493	14	1.0%	2.8%
Education and health services	$34,613	1,435	1,495	60	4.2%	6.2%
Other services	$26,307	344	347	3	0.9%	2.4%
Retail trade	$25,011	860	845	-14	-1.7%	-2.3%
Leisure and hospitality	$21,184	610	608	-2	-0.4%	0.6%

Sources: Wages are from the insured employment series. Employment data are from the BLS.

While both New York and the U.S. have stabilized employment, neither has gained many jobs over the past few months.



Unemployment insurance is an essential part of the safety net for individual workers, particularly during periods of high unemployment and is intended to serve as an "automatic stabilizer".

- Over the last 3 years (2001-2003), 1.2 million New Yorkers have filed for Unemployment Insurance claims each year. This represents a 36.7% increase over the last 2 years of the expansion.

- While the overall job level stabilized during 2003, the number of people seeking unemployment insurance benefits was slightly higher in 2003 than in 2001, the year when net job loss was at its greatest.

- Initial unemployment claims filed by NYC residents rose sharply in 2001, then declined slightly in the past 2 years. For the balance of the State, claims rose by 30% in 2001, and continued to increase in 2002 and 2003. From 2000 to 2003, initial claims rose by 38% in NYC, but by 45.5% in the rest of the State.

New York has one of the lowest recipiency rates for unemployment insurance among major industrial states, and one of the highest exhaustion rates.

	Recipiency Rate	Exhaustion Rate
New York	**43.8%**	**57.9%**
California	46.0%	47.8%
Illinois	45.1%	43.3%
Massachusetts	62.8%	44.3%
Michigan	48.6%	34.9%
New Jersey	52.8%	58.2%
Pennsylvania	58.6%	35.0%
U.S.	42.0%	42.4%

Source: Economic Policy Institute (EPI) analysis of BLS data. Data are for 2002.

Despite the continued crisis of joblessness, the Federal Government failed to renew the 13-week extension of unemployment benefits.

- From March 2002 when federal extended benefits began through October 2003, 640,000 New York workers received a total of $1.6 billion in federal benefits.
- However, unless the extended federal program is renewed, nearly 175,000 New Yorkers will be denied federal benefits during the first half of 2004. Their extended federal benefits would have totaled an estimated $465 million.

New York State needs to reform its unemployment insurance program so that a greater percentage of unemployed workers receive compensation when thrown out of work.

- More low-wage workers would qualify if eligibility requirements were based on hours worked rather than earnings, and if the Labor Department more regularly used the "alternate base period".
- Access could be improved by broadening translation services as California, Massachusetts and Washington have, and by making the claims system less complicated and more user-friendly.
- The adequacy of benefits should be improved by indexing the maximum benefit to changes in average weekly wages, and by raising benefit levels for low-wage workers above the current cap of 50% of past wages.
- The taxable wage base should be raised and indexed to make UI taxes more progressive and to improve the health of the UI trust fund.
- The state should adopt the "total unemployment rate" trigger for extended benefits.

"Together, we helped create almost 500,000 new jobs since 1995. Let's work together to create one million new [private sector] jobs by the end of the decade."

"A family feels a greater sense of freedom when it has the security of a good-paying job. That's why building a strong economic climate that creates good jobs is one of our highest priorities."

-- Governor George Pataki in his State of the State Address, January 7, 2004

A million new *good jobs* by the end of the decade is an important and laudable goal. There have been three periods since 1950 when New York State has added a million jobs, or close to it: the 1960s, 1980s and 1990s. These periods have typically run 8 or 9 years in length. The Governor set his goal of a million private sector jobs by "the end of the decade" -- that allows for 7 years from 2003 to 2010.

With annual population, labor force, and employment growth rates in the range of what New York experienced during the two most recent expansion periods -- from 1982 to 1989, and from 1992 to 2000 -- the Governor's numerical job creation goal is theoretically achievable. The Governor needs to tell us what actions the State will take to move us toward that goal beyond the tax cuts that he touts as having been responsible for "nearly a half million new jobs" since 1994.

The Governor's goal of 1 million new good jobs by the end of the decade is an excellent opportunity to raise questions:

- where within the State this job growth will take place?
- what steps will be taken to ensure that these are good, family-supporting jobs?
- how will the State will better monitor its economic development efforts to make them more accountable to taxpayers?

During the expansions of the 1960s and the 1980s, the upstate area accounted for about 40% of job growth, roughly in line with its share of the population and jobs. In the expansion from 1992 to 2000, however, upstate accounted for only 25% of the net job gain.

Because upstate has under-utilized infrastructure and much more affordable housing, among other attributes, its is reasonable to expect that the State will more effectively channel growth to the upstate regions. And from a sound land-use and fiscal planning perspective, growth upstate should be focused on the cities, and not allowed to continue sprawling outward to suburban and rural areas.

For jobs to be "family-supporting", they need to be well-paying and secure, and ones that offer benefits such as employer-provided health insurance and pension coverage. For the past decade, and longer in the case of employer-provided benefits, there has been a steady erosion in the quality of jobs available in New York State. The table on the next page shows that the industries that have increased their share of all jobs over the past 2 years pay, on average, 38% less than the industries losing employment share. In our 2001 The State of Working New York, we noted that employer-provided health coverage in NYS had fallen from 72% in the late 1970s to 57% by the late 1990s, and employer-provided pension coverage fell from 54% in the late 1970s to 47% in the late 1990s.

New York State's Job Gains and Losses, and Job Share Gains and Losses, by Industry

November 2001 to November 2003

				Job Gain or Loss		Job Share Gain or Loss	
Industry	**Employment Nov. 2001 (in 000s)**	**Employment Nov. 2003 (in 000s)**	**Average Annual Pay in Industry**	**Change (000)**	**Gain or Loss?**	**Change**	**Gain or Loss?**
Educational and Health Services	1,468.1	1,516.0	$34,613	47.9	gaining jobs	+0.72%	gaining share
Leisure and Hospitality	621.0	648.3	$21,184	27.3	gaining jobs	+0.39%	gaining share
Retail Trade	885.7	890.3	$24,985	4.6	gaining jobs	+0.15%	gaining share
Other Services	345.5	351.5	$26,307	6.0	gaining jobs	+0.11%	gaining share
Government	1,503.2	1,497.4	$42,947	-5.8	losing jobs	+0.09%	gaining share
Construction	337.6	341.2	$47,721	3.6	gaining jobs	+0.08%	gaining share
Financial Activities	701.7	701.4	$103,744	-0.3	losing jobs	+0.07%	gaining share
Subtotal, industries gainining job share [1]			**$34,081**	**83.3**		+1.60%	
Natural Resources and Mining	5.5	5.2	$26,190	-0.3	losing jobs	-0.00%	losing share
Transportation and Utilities	273.9	266.9	$43,410	-7.0	losing jobs	-0.05%	losing share
Wholesale Trade	362.7	351.8	$55,917	-10.9	losing jobs	-0.09%	losing share
Manuf Non Durable Goods	290.2	265.9	$42,763	-24.3	losing jobs	-0.26%	losing share
Professional and Business Services	1,074.3	1,041.4	$58,626	-32.9	losing jobs	-0.27%	losing share
Information	319.7	280.1	$66,569	-39.6	losing jobs	-0.43%	losing share
Manuf Durable Goods	392.9	347.6	$48,924	-45.3	losing jobs	-0.49%	losing share
Subtotal, industries losing job share [1]			**$54,537**	**-160.3**		-1.60%	
TOTAL	**8,582.0**	**8,505.0**	**$46,328**	**-77.0**			

Note: Employment data are not seasonally adjusted. Wage data are for 2002 from the Insured Employment series.

1. The average wage for the growing and declining industry groups was computed by weighting the industry average wage by each industry's share of the change in the job share for that group.

Source: FPI and EPI analysis of U.S. Bureau of Labor Statistics data.

Twelve States and the District of Columbia Already Have Minimum Wages Above the Current Federal Minimum Wage

(as of January 1, 2004)

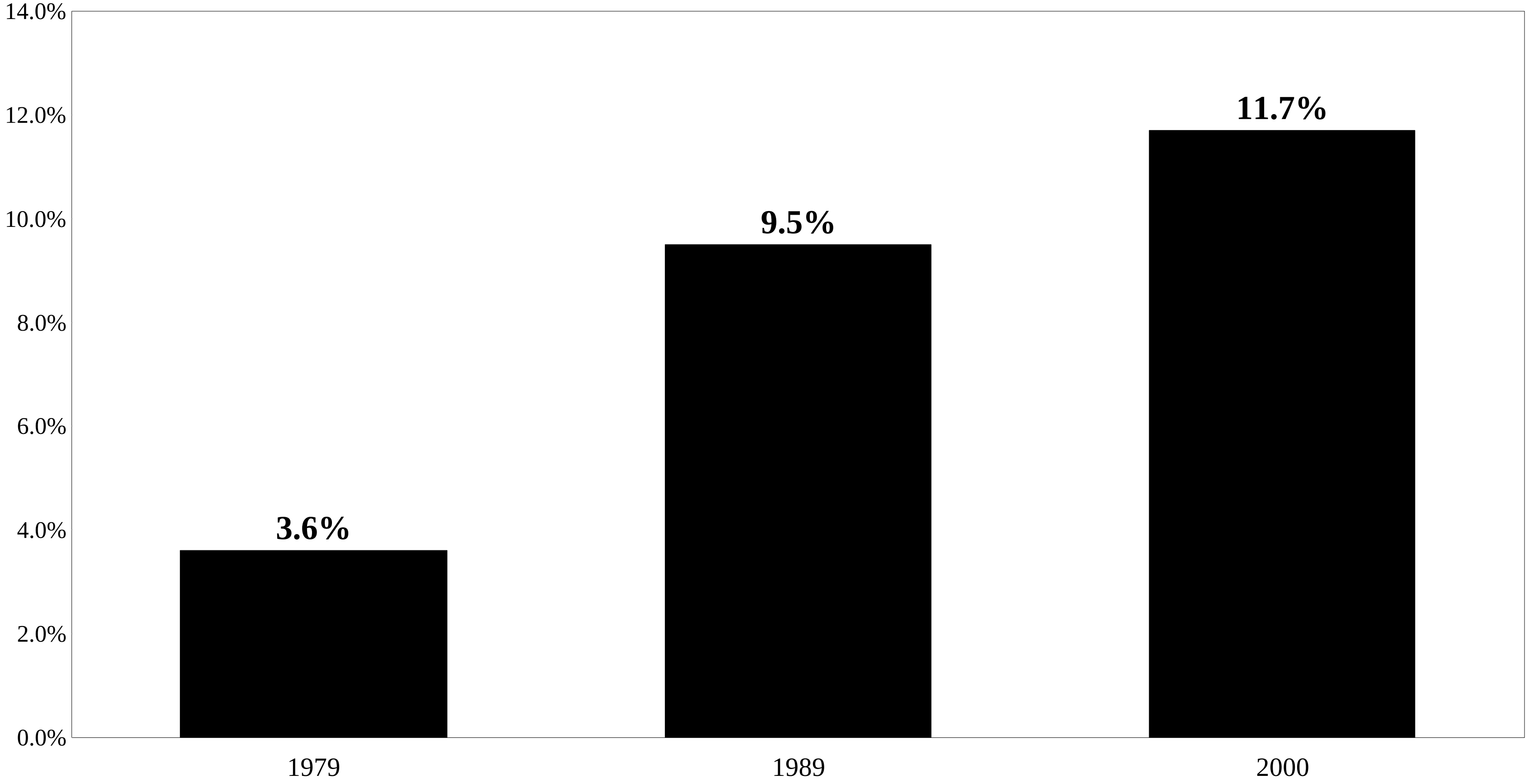
State	Minimum Wage
Washington**	$7.16
Alaska	$7.15
Connecticut	$7.10
Oregon**	$7.05
California	$6.75
Massachusetts	$6.75
Rhode Island	$6.75
Vermont*	$6.75
Hawaii	$6.25
Maine	$6.25
Delaware	$6.15
District of Columbia	$6.15
Illinois*	$5.50

* Illinois' minimum wage will increase to $6.50 on January 1, 2005. Vermont's minimum wage will increase to $7.00 on January 1, 2005.

** Oregon and Washington index their minimum wages to account for annual increases in the cost of living.

A Growing Share of New York's Workers Are Being Paid Very Low Wages

Share of Workers Earning Less Than $7/Hour at the Last Three Business Cycle Peaks (Hourly wages in September 2003 $)



Source: Fiscal Policy Institute analysis of CPS ORG data obtained from EPI.
Note: Adapted from similar chart developed for NYC's 2002 living wage campaign. See: Mark Levitan and Robin Gluck. "Who Needs a Living Wage?" Data Brief #5, Community Service Society of New York, April 2002.

Raising the minimum wage to $7.00 an hour would directly benefit nearly 700,000 New York workers now making between $5.15 and $6.99, and likely would boost the wages of many of the 500,000 workers making between $7 and $8 an hour.

- The majority of those benefiting directly are adults (74%) and people who work more than half-time (78%).

- Because women and people of color tend to be more concentrated in industries and occupations paying lower wages, they are over-represented among those who stand to benefit from a minimum wage increase. Of those who would directly benefit, 61% are women, 20% are Hispanic, and 15% are African-American.

- Lower income households disproportionately will benefit. One third of the earnings gain will accrue to the bottom 20% of households although they receive only 5% of all wage earnings. The lowest earning 40% will receive 56% of the benefit.

- The earnings of New York's minimum wage workers are vital to the total wage earnings received by their families. Their wages provide half of total family wage earnings in families with minimum wage workers. More than a third of all families with a minimum wage worker rely solely on the earnings from minimum wage employment.

Appendix A: Progressive, Proportional and Regressive Tax Systems

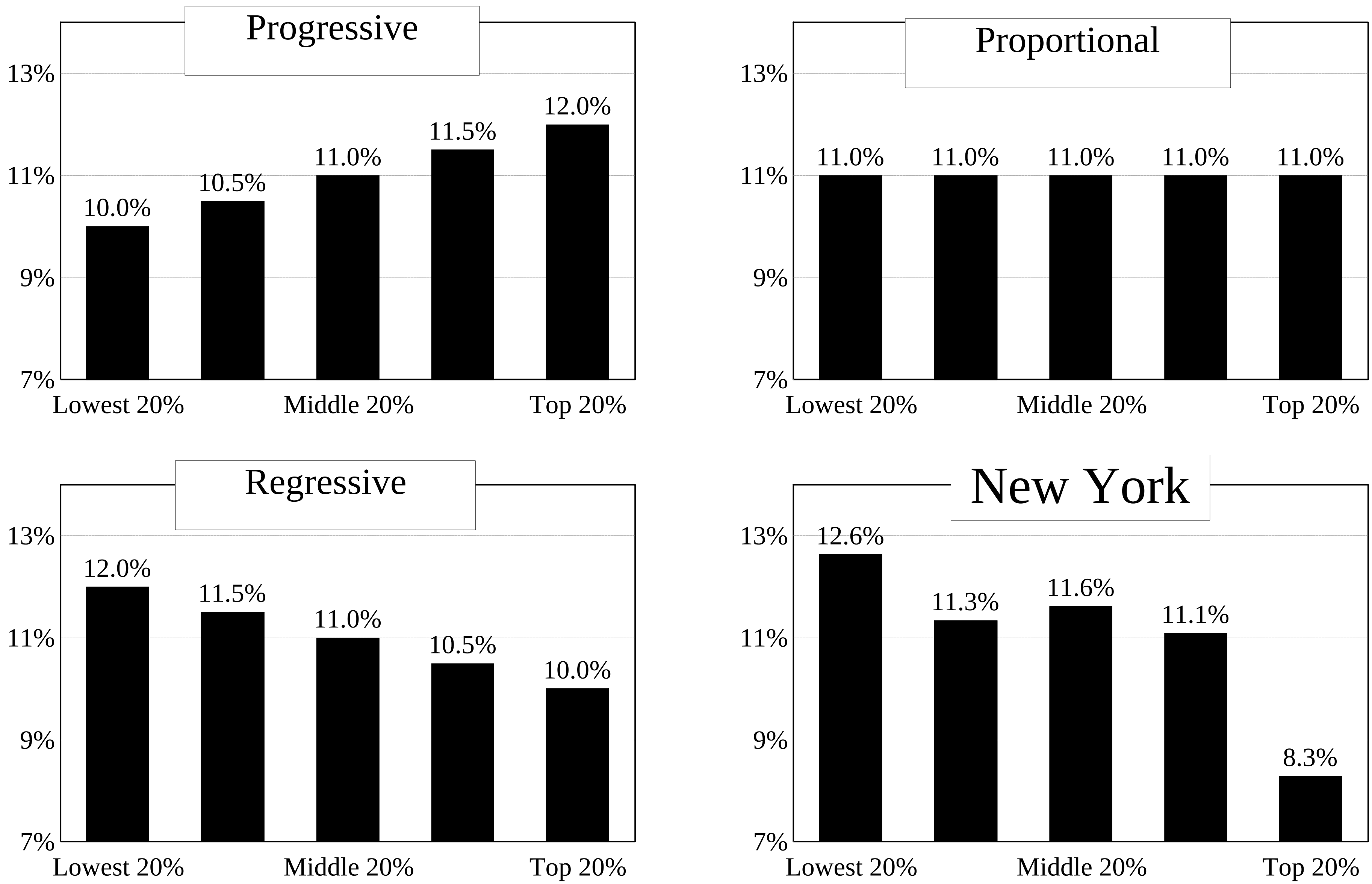
- A regressive tax system is one in which the portion of a household’s income that goes to taxes decreases as its income increases. In other words, a regressive tax system is one in which wealthy households pay a smaller share of their incomes in taxes than do lower income households.

- A progressive tax system is one in which the portion of a household's income that goes to taxes increases as its income increases.

- A proportional tax system is one in which all households, regardless of their income levels, pay about the same portion of their incomes in taxes.

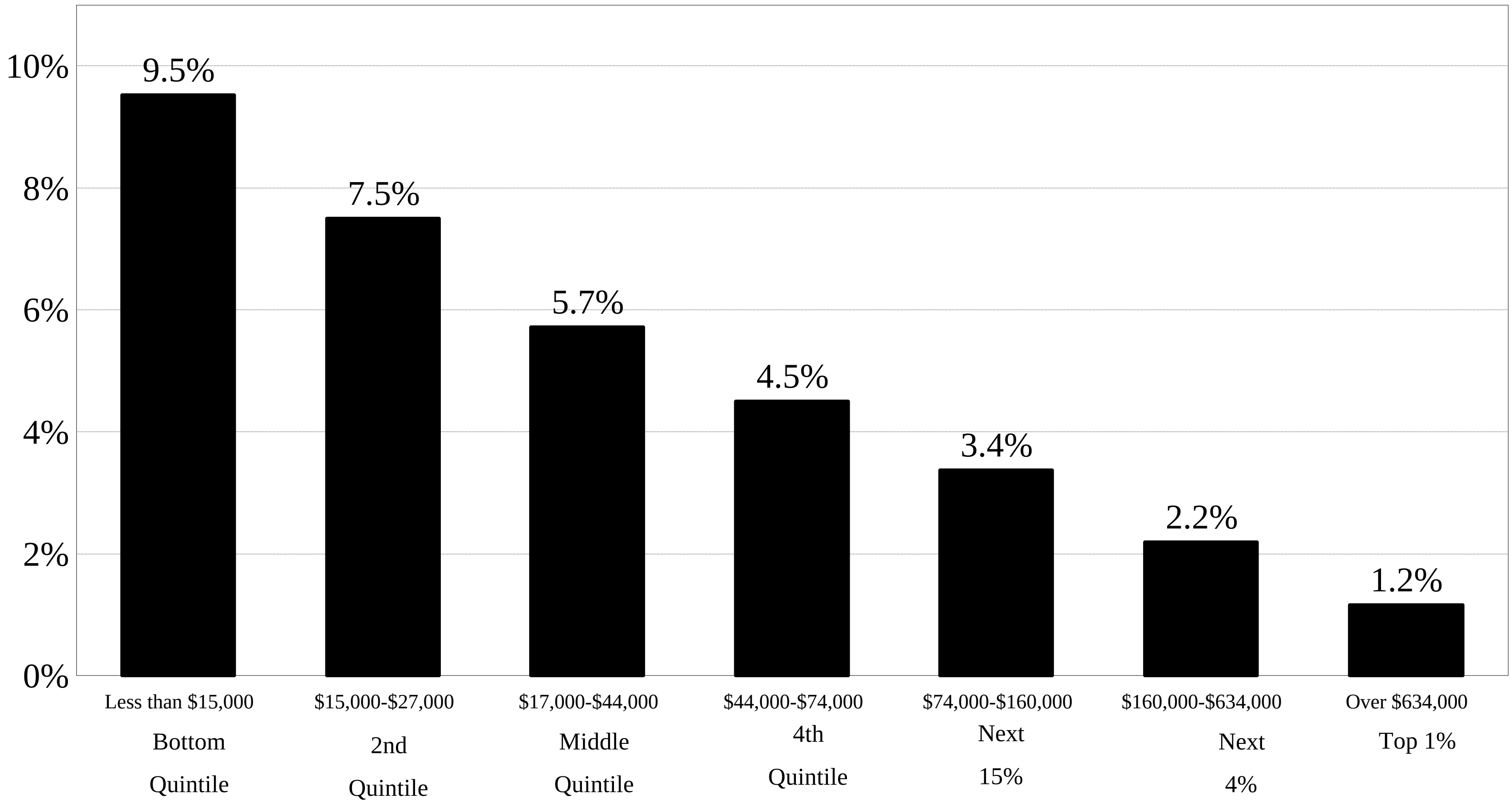
- While it is interesting to note if an individual tax is regressive, proportional, or progressive, the more important question is whether the tax system as a whole is regressive, proportional, or progressive. For most states, the question is whether or not the progressivity of its personal and corporate income taxes and its estate tax balance out the regressivity of its consumption, excise and property taxes.

Progressive, Proportional and Regressive Tax Systems



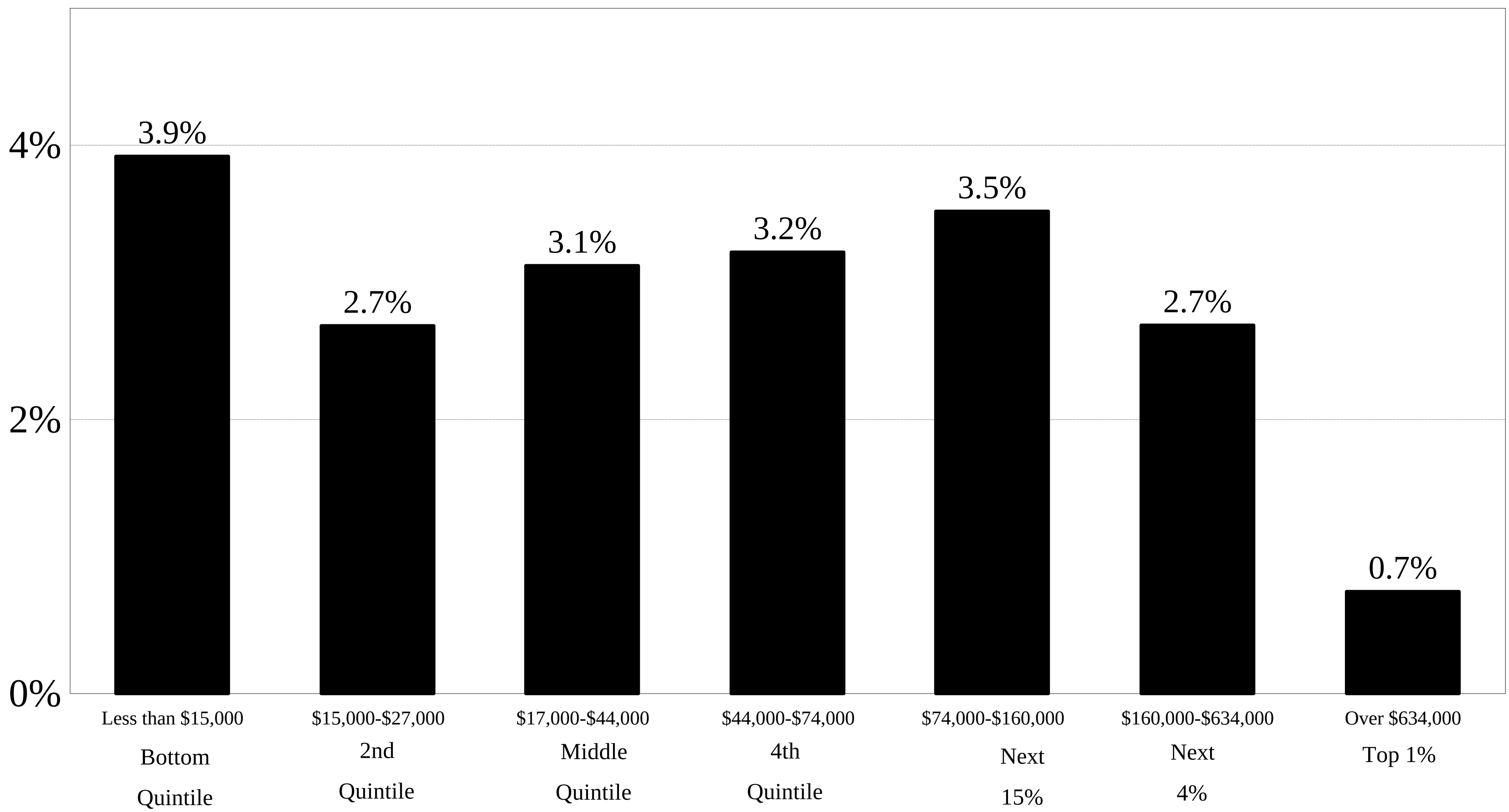
New York figures are from the Institute on Taxation and Economic Policy for 2002 tax law at 2000 income levels for nonelderly taxpayers, after federal offset.

New York's sales and excise taxes are inversely



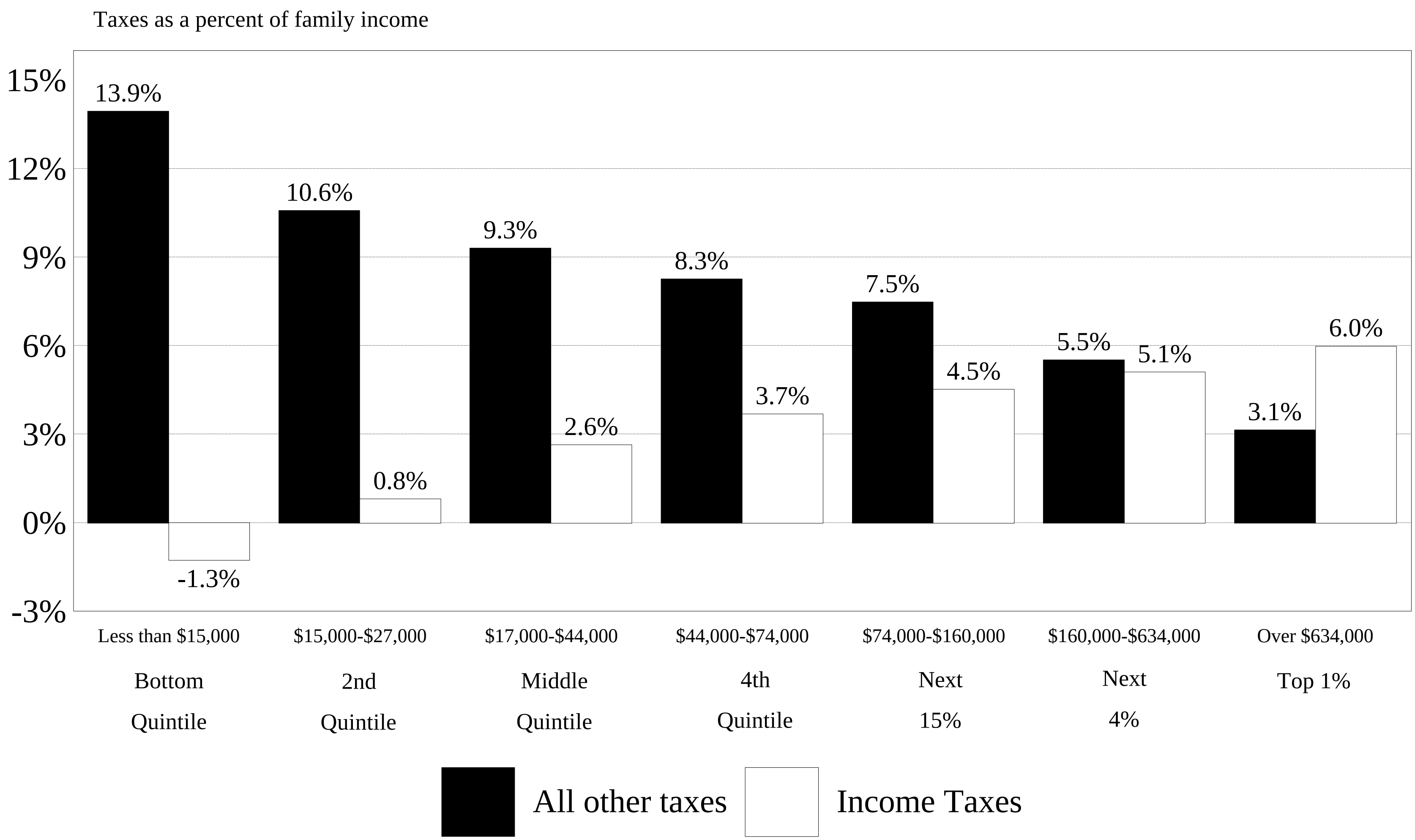
Source: Institute on Taxation & Economic Policy, 2003. Table shows 2002 tax law at 200 income levels for nonelderly taxpayers .

New Yorkers' residential property tax burdens are not systematically related to income.



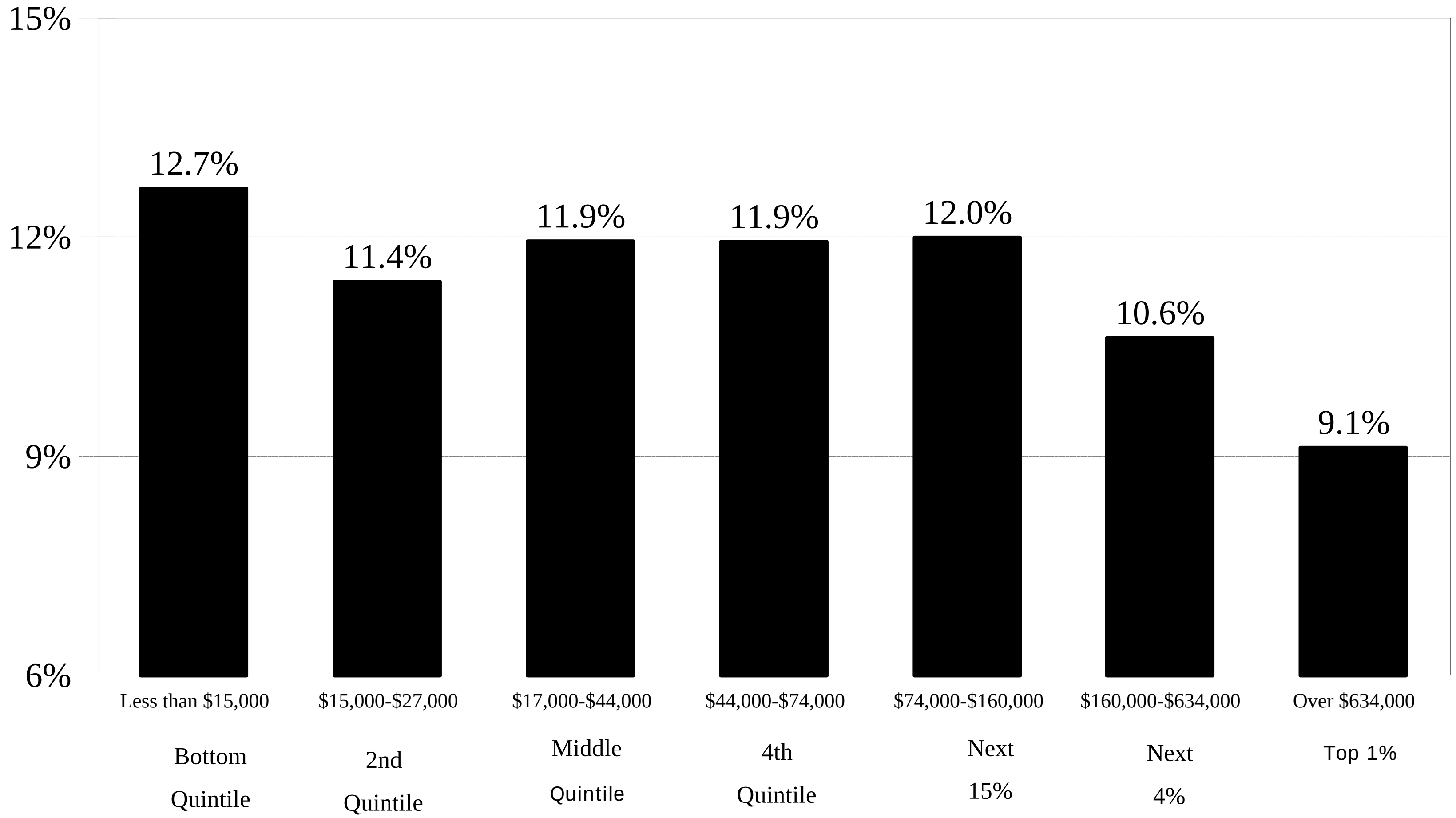
Source: Institute on Taxation & Economic Policy, 2003. Note: Table shows 2002 tax law at 2000 income levels for nonelderly taxpayers, before federal offset.

New York State's personal income tax helps to balance the regressivity of the rest of the tax system.



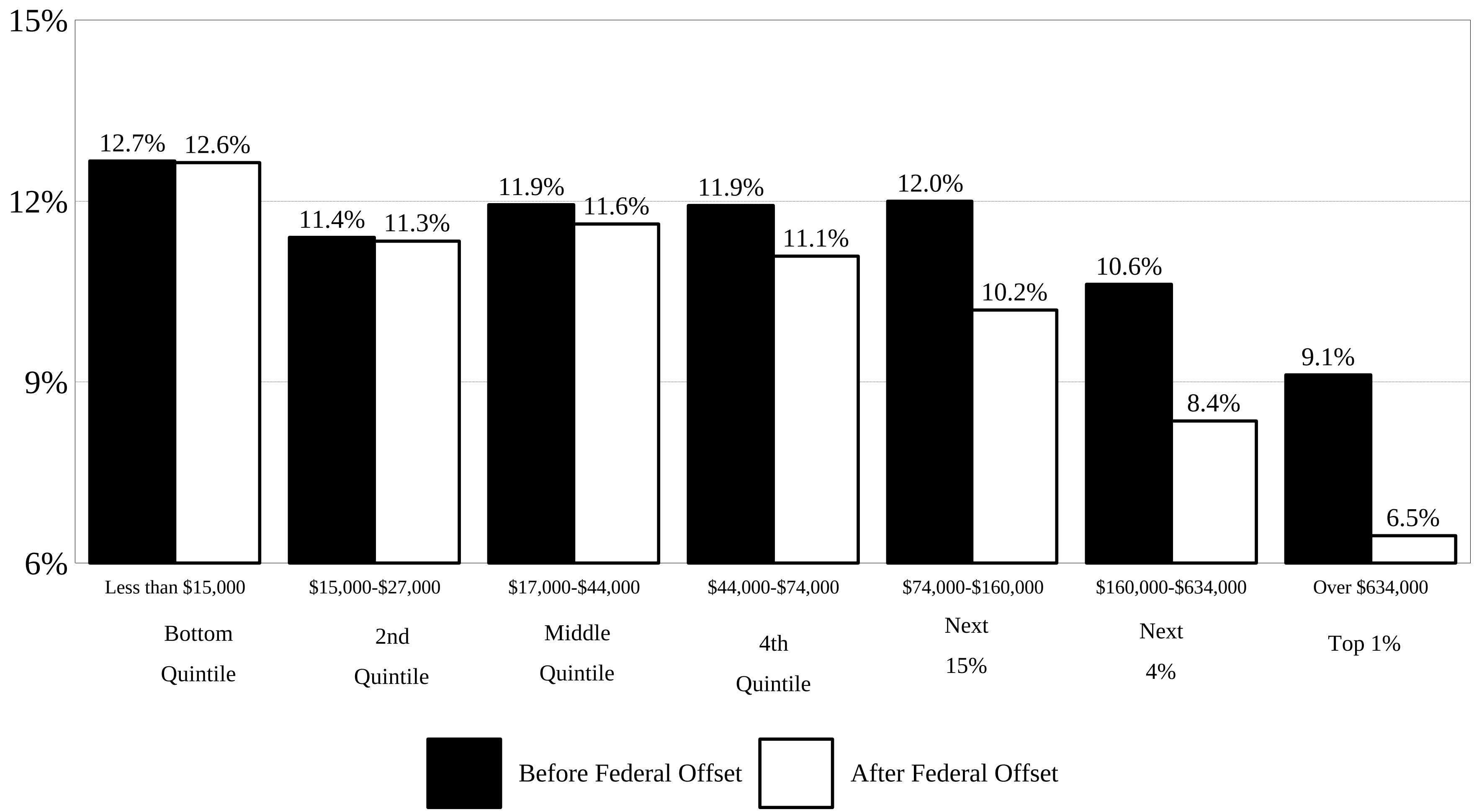
Source: Institute on Taxation & Economic Policy, 2003. Table shows 2002 tax law at 2000 income levels for nonelderly taxpayers,. before federal offset.

Overall, the wealthiest 5% of households pay a much smaller share of their income in state and local taxes than do all other New Yorkers.



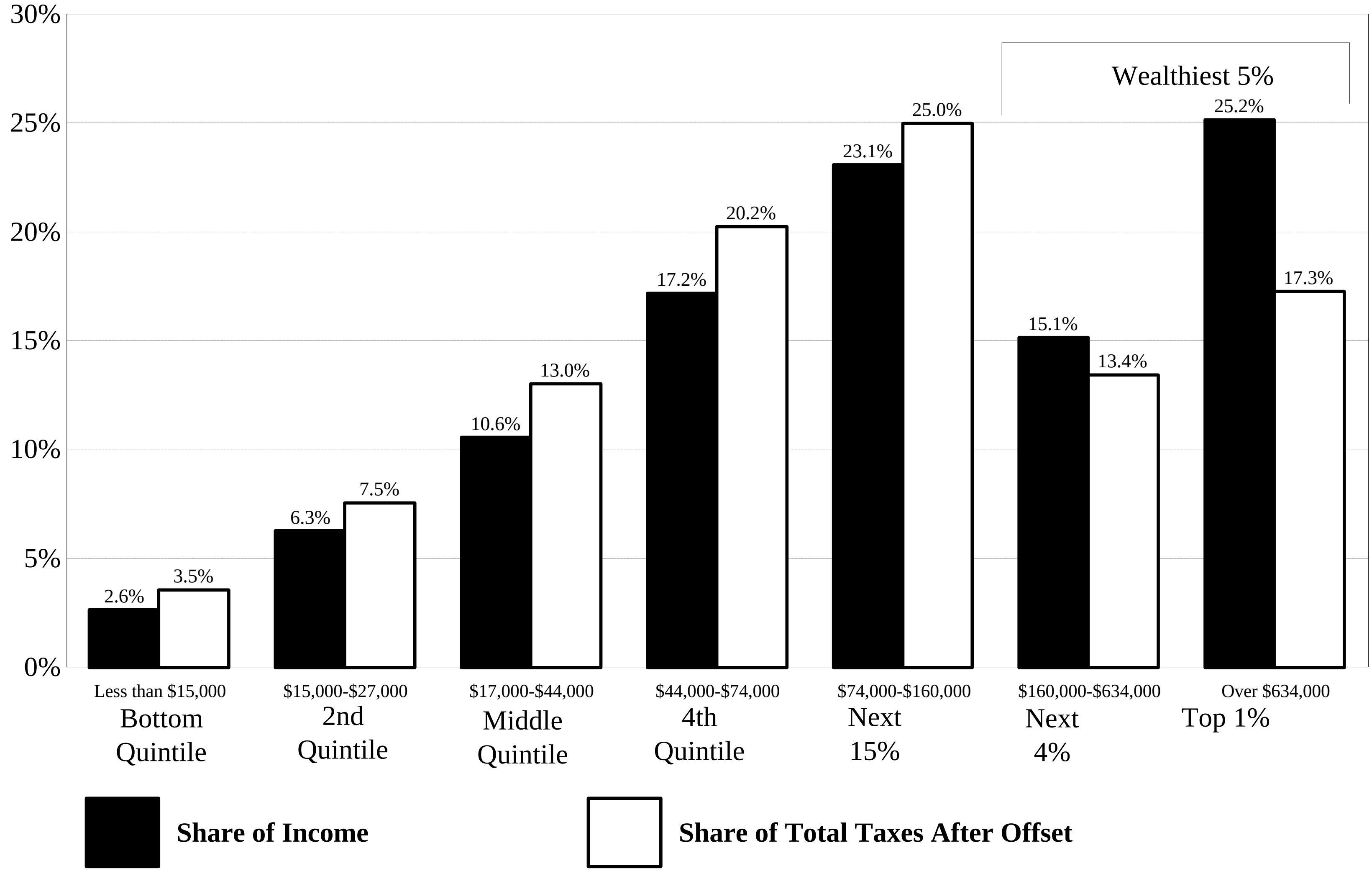
Source: Institute on Taxation & Economic Policy, 2003. Table shows 2002 tax law at 2000 income levels for nonelderly taxpayers, before federal offset.

When federal deductibility is taken into consideration, the differences are even greater.



Source: Institute on Taxation & Economic Policy, 2003. Table shows 2002 tax law at 2000 income levels for nonelderly taxpayers, before federal

Taking federal deductibility into consideration, the wealthiest 5% of New York's families have over 40% of the income but carry less than 31% of the state-local tax burden.



Source: Institute on Taxation & Economic Policy, 2003. Table shows 2002 tax law at 2000 income levels for nonelderly taxpayers, after federal offset.
The percentages for the seven income groups add to 100%.