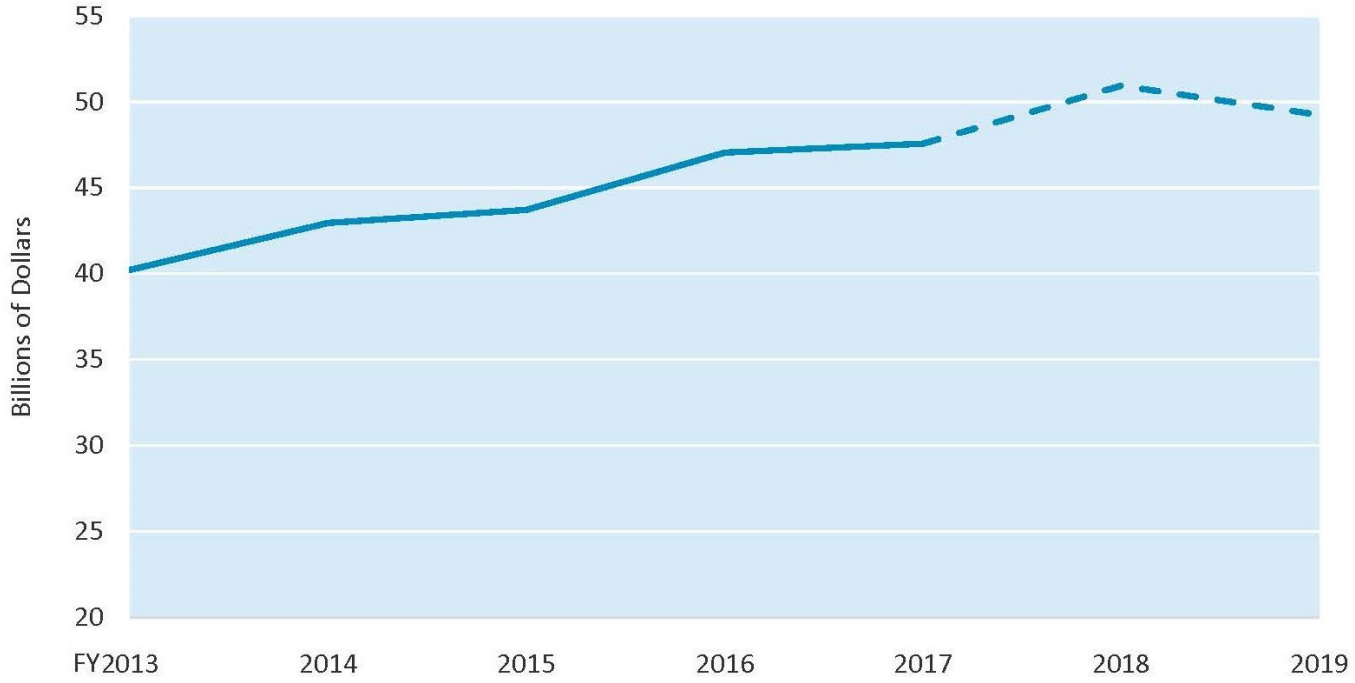
Financial Plan

The budgetary situation this year presents a number of very serious challenges.

First, the State of New York has a budgetary gap of $4.4 billion. There are several reasons for the gap, the biggest single reason is the 3.3 percent decline in the personal income tax (PIT) collections. New York State has been overly ambitious in its tax reductions, continuously lowering personal income tax rates over many years to what is currently a historical low level. This has, unsurprisingly, meant a significant decline in state revenue, opening a predictable budget gap. The PIT accounts for about 60 percent of the state's tax receipts. The shortfall in PIT stands at -$1.69 billion this year and projected to grow to -$2.5 billion next year. Therefore, unless the tax collections increase spontaneously, the state needs an appropriate plan to approach the matter of deficit reduction.

Fig 1. Personal Income Tax



FY 2019 Executive Budget Financial Plan (page 10).

Second, the new federal tax law, the Tax Cuts and Jobs Act of 2017 (TCJA), introduces a new fiscal environment that could pose real problems for New York's taxpayers and economy unless meaningful adjustments are made at the state level.

Third, the adoption of the federal tax law is projected to cost $1.5 trillion in lost revenue at the federal level. There is a high probability for the near future where this may prompt the federal government to cut back on state funding or reform some of its programs, such as Medicaid and social services. If it happens, it will have a profound negative

impact on New York. After sending much more to Washington, New York receives back over $70 billion annually in federal funds, of which over $37 billion goes to Medicaid. Thus, the long-term state budget gap may be much larger than what most current projections show.

In order to avoid being short-sighted and imprudent, and in anticipation of looming financial hits from the federal government or from eventual potential downturns in the market, New York should seek to optimize its fiscal policy with a view to further increasing revenues to preserve and expand services for the state's most vulnerable populations. The solution, however, is not austerity. The Executive Budget proposes highly limited and unnecessarily restricted spending growth. Austerity is an unimaginative policy stance; it is not a hallmark of good governance. A better solution is to sustainably raise the revenues adequate to meet the state's needs.

Spending Growth

The state of New York has enjoyed quite a bit of growth since the Great Recession.

Fig 2. While the Economy is Expected to Continue Its Slow Growth in 2018, the Forecast is for Better Economic, Wage, and Income Growth in Out-Years

Source: NY FY2019 Economic and Revenue Outlook, Economic Backdrop section

New York City real estate benefitted from historically low interest rates and the financial sector used the forced consolidation and bail-out cash to its advantage. Overall, NYC survived the depths of the Great Recession as one of the most attractive job markets in the country where despite increasing polarization the median income has been growing steadily since 2008.

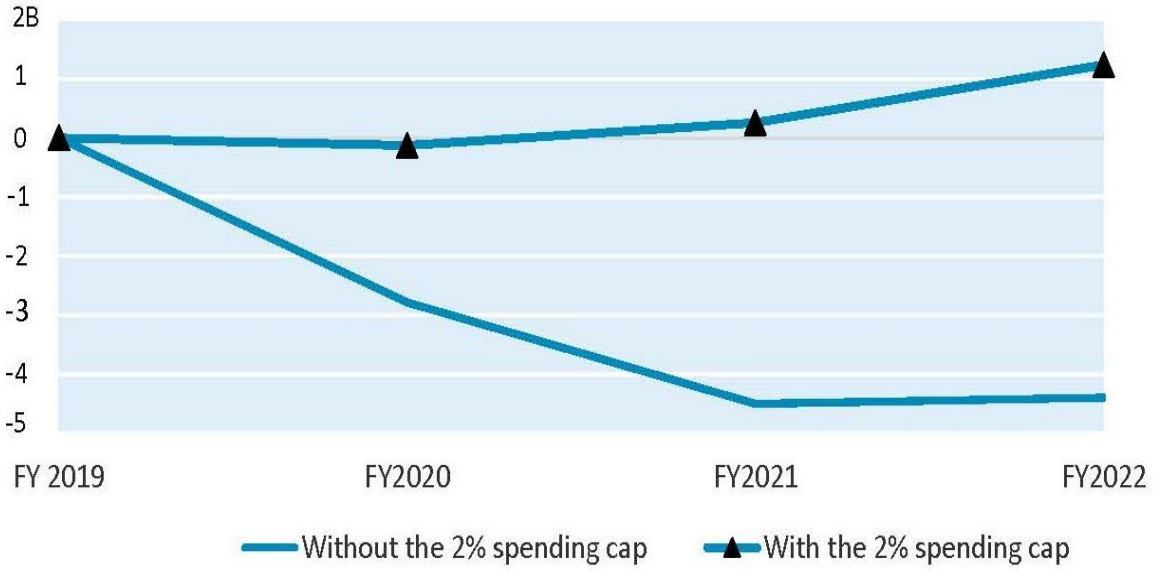
Austerity was never a good approach to state budgeting, but it is now stretched beyond its limit. For one thing, further draining of resources from state services is hardly possible without rapid deterioration of quality, since most of the low-hanging-fruit efficiencies have been picked. Further cuts are more likely than before to cripple operations and lower output quality. In addition, the economic environment has changed and the state needs to face new challenges and adapt to the shifting legislative and policy landscape.

Governor Cuomo's Executive Budget continues to be constrained by a self-imposed two-percent spending growth cap. The total state operating funds' spending measures are projected to increase by $1.85 billion or 1.9 percent during FY 2019. (The total of all government spending—which also includes capital funds and federal aid—is expected to grow by $3.75 billion or 2.3 percent.) Over the years the two-percent cap has become Governor Cuomo's trademark budget policy principle, meant to signify his strict adherence to fiscal discipline. But the self-imposed austerity does not represent good governance at a time when the state population is growing and needs from poverty relief to transit investment are going unmet.

While the overall state operating funds expenditure is proposed to increase by only 1.9 percent, just under the two-percent cap, there are spending categories the governor expects to grow by a lot more and a lot less. Medicaid spending is projected to increase the most among all spending categories, rising by $1.23 billion or 6.5 percent. Other notable increases are in School Aid, $769 million or 3.0 percent, and Higher Education, $228 million or 8.1 percent. Overall growth in Local Assistance is up by a mere 0.9 percent or $619 million, while at the same time, the State Operations spending is up by $644 million or 3.4 percent. Transportation will see the largest decrease in spending by both the dollar amount (-$1.06 billion) and growth rate (-21 percent), followed by Mental Hygiene (-$199 million or 8.4 percent).

The state's deficit reduction plan mainly relies on adherence to the two-percent spending benchmark. If the spending growth is limited at two percent, then, according to the financial plan, the executive budget gap will be positive by FY 2021 at $256 million and will increase to reach $1.24 billion by FY 2022. The proposed plan also features a number of modest revenue actions that are projected to yield just over $1 billion in FY 2019, followed by $1.4, $1.3 and $1.2 billion in Fiscal Year 2020, 2021 and 2022 respectively. The projected 2022 surplus, it should be noted, is entirely dependent on the proposed revenue actions. If those are not enacted, even with the unforced austerity there will be no new capacity for meaningful spending maneuvers in the short- to medium-run.

Fig 3. Projected Budget Gaps (Surpluses) with and without 2% cap, to 2022



Source: FY 2019 Executive Budget Financial Plan (page 10).

Proposed Revenue Plan

The executive budget proposal lists a few revenue raisers totaling just over $1 billion. The revenue plan is rather timid and does not go nearly far enough to address the state's budget problems. In fact, the plan presents an array of missed opportunities to advance a truly progressive vision.

Health Insurance Conversions and Similar Transactions ($500 million)

This is largest revenue raiser. The Division of Budget (DOB) expects to see for-profit companies buy not-for-profit health insurance companies. This activity, if taxed, is estimated to generate $500 million annually over the next four years.

Healthcare Insurance Windfall Profit Fee ($140 million)

The governor seeks to recapture $140 million annually of the health insurance companies' corporate tax savings produced by the federal tax law. The revenue will be used to pay for vital health care services.

Opioid Epidemic Surcharge ($127 million)

The governor proposes a 2-cent per milligram surcharge on the active opioid ingredients in prescription drugs. All revenues are to be used for the Opioid Prevention, Treatment and Recovery Fund.

Discontinue Energy Service Company (ESCO) Sales Tax Exemption ($90 million)

This measure eliminates the sales tax exemption on the non-residential transmission and distribution of gas and electricity for commercial customers. After bringing $90 million in FY 2019, the measure is projected to yield $120 million in subsequent years.

Defer Business Related Tax Credit Claims ($82 million)

Business tax credits over $2 million are deferred through FY 2020, and become refundable at 50 and 75 percent in FY 2021 and 2022 respectively. It is expected to generate $82 million in revenue in FY 2019, $278 million in 2020, $199 million in 2021, and $164 million in 2022.

Internet Fairness Conformity Tax ($75 million)

Expand the tax on internet sales to New York residents that large online retailers like Amazon already pay to include all online marketplaces. The governor projects this measure will generate $75 million in FY 2019 and $150 million thereafter.

Improve Cigar Tax Enforcement ($12 million)

Change the definition of "wholesale price" for manufacturers and distributers of cigars so that the industry cannot use a pricing survey to determine the tax on its own products. The projected revenue is $12 million FY 2019 and $23 million in the following years.

All Other Revenue Actions ($9 million)

Among them: a new "health tax" of 10 cents per fluid milliliter on vapor products, an increase in the vending machine food and drink sales tax exemption, and a Hire a Vet Tax Credit extension to 2020. The governor expects these to result in $9 million in FY 2019, $21 million in FY 2020 and turn negative becoming -$11 million and -$10 million in FY 2020 and 2021 respectively