

FISCAL POLICY INSTITUTE

11 Park Place, Suite 701, New York, NY 10007

212-721-5624 www.fiscalpolicy.org

Testimony of
James A. Parrott, Ph.D.
Deputy Director and Chief Economist
Fiscal Policy Institute

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New York City Council
Finance Committee

Mayor's Executive Budget Proposal

New York City
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Good afternoon, my name is James Parrott, Deputy Director and Chief Economist of the Fiscal Policy Institute (FPI). The Fiscal Policy Institute is a nonpartisan research and education organization that focuses on the broad range of tax, budget, economic and related public policy issues that affect the quality of life and the economic well-being of New York City and State residents. FPI regularly prepares reports on the state of the New York City economy and the economic condition of workers and their families, and on city budget and tax policy issues. Thank you for the opportunity to testify today.

The Great Recession might be over in a technical sense for the nation and New York City, but the recovery path will be rocky and long. And while it's true that New York City lost proportionately fewer payroll jobs in this recession than in the two previous downturns in the early 1990s and the early 2000s, by other measures such as the falloff in total wages or the rise in joblessness among city residents, this recession is every bit as bad as, or worse than, the two that preceded it.

Leaving aside the volatile finance sector, total non-finance wages in New York City fell by five percent in 2009, a much steeper decline than during the two previous downturns. Many more workers suffered pay cuts and/or were forced to work fewer hours during the current recession than during the last two. With wages dropping that much, households have sharply curtailed their spending in neighborhood shops and restaurants. From early 2008 until December of 2009, the number of jobless city residents more than doubled to over 400,000.¹

¹ See Fiscal Policy Institute, *Is the Recession Over in New York?* May 10, 2010.
http://www.fiscalpolicy.org/FPI_IsTheRecessionOverInNewYork.pdf

While citywide, overall unemployment hovers around the 10 percent rate, in central and south Bronx, central and east Brooklyn, Harlem, and Washington Heights, unemployment rates among blacks and Hispanics are 15 to 20 percent, three or four times the unemployment rates among non-Hispanic whites on the Upper East and West Sides and in brownstone Brooklyn.²

There has been a sharp disconnect between the fortunes of Wall Street and Main Street New York City during this Great Recession.³ New York City's job losses have been heavily concentrated in moderate- and middle-income paying sectors largely populated by city residents. As the attached table indicates (see Chart 1), the brunt of job loss has occurred in construction, manufacturing, trade and transportation, administrative and building services, and in the government sector.

In fact, there has been a steeper decline in local government employment in New York City over the past two years than there has been in total private employment. New York City local government employment has dropped by nearly 20,000 or 4.3 percent from April 2008 to April 2010, compared to a 3.4 percent decline in total private employment in New York City.⁴ And of course, the Mayor's Executive budget calls for the reduction of several thousand more city employees.

Meanwhile, Wall Street chalked up record profits in 2009—in fact, three times the previous record and more than the combined profits of the four years of the housing bubble from 2003 to 2007 (see attached Chart 2). The State Comptroller estimates that the 2009 level of profitability translated into \$20 billion in bonus payments to New York City-based Wall Street employees.

It is critical that the City balance its budget in a way that does not unduly burden neighborhoods that are reeling, and will be reeling further, from the effects of the recession for some time to come. The city's poverty rate was already 22 percent in 2008, before the recession set in, and the social safety net has become badly frayed over the years. The Mayor's Executive Budget proposal targets a wide range of essential City services for cuts—ranging from child care centers to senior centers, afterschool programs and libraries, school nurses and transitional employment positions in the Parks Department. The impact of these cuts is concentrated in neighborhoods that can ill afford to lose support services to low- and moderate-income city residents.⁵ And the proposed cuts come on top of several rounds of previous cuts since early 2008.

New York City needs a more balanced approach to closing large budget gaps and balancing its budget. The City needs to look at the revenue side of the equation as well. Since 2002, when the City has sought to increase revenues to stave off more devastating budget reductions, it has largely turned to regressive taxes—the 2002 18.5 percent increase in the property tax and the

² See Fiscal Policy Institute, *New York City: Divergent Fates by Neighborhood and Race and Ethnicity*, December 2009. http://www.fiscalpolicy.org/FPI_NeighborhoodUnemployment_NYC.pdf.

³ James A. Parrott, "New York City: A Tale of Two Recessions," *Challenge*, May/June 2010.

⁴ New York State Labor Department non-agricultural employment data, seasonally adjusted by Fiscal Policy Institute.

⁵ A recent article in the New York Times article illustrated the concentrated impact of proposed service cuts in the Carroll Gardens-Boerum Hill neighborhood of Brooklyn where the unemployment rate is 27 percent among blacks and 14 percent among Hispanics. David W. Chen, "Budget Cuts Hit a Brooklyn Area Over and Over," *The New York Times*, June 5, 2010. <http://www.nytimes.com/2010/06/05/nyregion/05cuts.html>

2009 12.5 percent increase in the city's sales tax rate have accounted for most of the higher taxes. The City's personal income tax was increased in a progressive manner on a temporary basis from 2003 to 2005. These changes have contributed to the overall regressive nature of how the local tax burden is shared in New York City.

As Chart 3 indicates, relative to household income levels, the wealthiest one percent of the population in New York City pays a lower share of its income in local income, sales and property tax than less fortunate New Yorkers.⁶ While the wealthiest one percent pay about half of the city personal income tax, what is often overlooked is the fact that they receive 45 percent of all income, and their incomes nearly tripled (+188 percent) from 2002 to 2007. On the other hand, the increase in the total incomes of the bottom 70 percent of New York City's population, basically those people in households with incomes under \$50,000, experienced a collective gain in incomes of 21 percent from 2002 to 2007, barely keeping pace with inflation over that period. The top 1 percent pays much smaller shares of their income in sales and property tax than do less wealthy New Yorkers.

The City could go a long way to redressing this regressive picture by reforming its personal income tax structure to moderately increase tax rates at the top and increase tax credits for low- and moderate-income households to lighten tax burdens among those with the least income. Income tax reform along these lines, which would require Albany approval, could generate roughly \$1 billion annually. The exact amount depends on the how taxes were increased at the top, and the configuration of changes to the City's three tax credits that provide relief to low-income households (the earned income tax credit, the child and dependent care credit and the New York City household credit).

Another revenue option that should be carefully examined is eliminating the "carried interest" exemption on the City's Unincorporated Business Tax (UBT).⁷ This is a loophole that costs New York City upwards of \$100 million yearly and results in the perverse result that the city's truly small businesses are asked to pay a higher effective UBT tax rate than hedge funds that generate hundreds of millions of dollars in fees for their principals. Hedge funds and private equity funds have grown tremendously in recent years and constitute a growing "shadow" banking sector in the U.S. The UBT helps to maintain a level playing field among large businesses across the various sectors of the city's dynamic commercial and financial economy. In 2004, 92 percent of UBT taxes were paid by business owners with over \$250,000 in profit. The UBT taxes the business income of highly profitable companies that happen to be organized as partnerships and limited liability companies. Should the carried interest exemption be eliminated, the additional tax liability will be moderated by the very generous 23 percent credit for UBT tax payments against New York City personal income tax liability.

⁶ The estimates on tax burden by income group are based on 2007 data on the city personal income tax, together with estimates from the Institute on Taxation and Economic Policy regarding the incidence of New York sales and property taxes. These estimates do not include the impact of water and sewer fees that are also regressive in their incidence and have nearly doubled since 2002.

⁷ For a thorough examination of this proposal, see Fiscal Policy Institute, *Re-thinking the New York City business Tax Treatment of Private Equity Fund and Hedge Fund "Carried Interest"*, April 15, 2008. http://www.fiscalpolicy.org/FPI_RethinkingTaxTreatmentOfCarriedInterest.pdf.

No one wants to pay higher taxes. The city and state tax burden is high in New York City. However, we need to keep in mind that the *value added* by the production of goods and services in New York City is extraordinarily high, and that this per worker productivity advantage relative to the U.S. average holds almost across the board. Excluding the finance and real estate sectors, the average value added per worker in New York City's private sector is 36 percent higher than the national average.⁸ New York City's dense concentration of economic activity—which also requires an extensive publicly-funded infrastructure and a high level of public services—is the main reason for this impressive productivity advantage.

The recession has taken a heavy toll on the livelihoods of hundreds of thousands of New Yorkers, and the adverse effects in further wage and job loss will persist for several months, if not years, to come. Adequately funded health, education, youth, and other social service-oriented public services are essential to maintain the quality of life for average New Yorkers. It is quite reasonable to ask those who have benefitted so greatly from the city's robust economy to share some of the burden of balancing New York City's budget.

Thank you for the opportunity to testify today.

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⁸ See Figure 9, Fiscal Policy Institute, *New York City: A Tale of Two Recessions*, November 29, 2009, p. 11. http://www.fiscalpolicy.org/FPI_NewYorkCitysTwoRecessions_20091119.pdf.

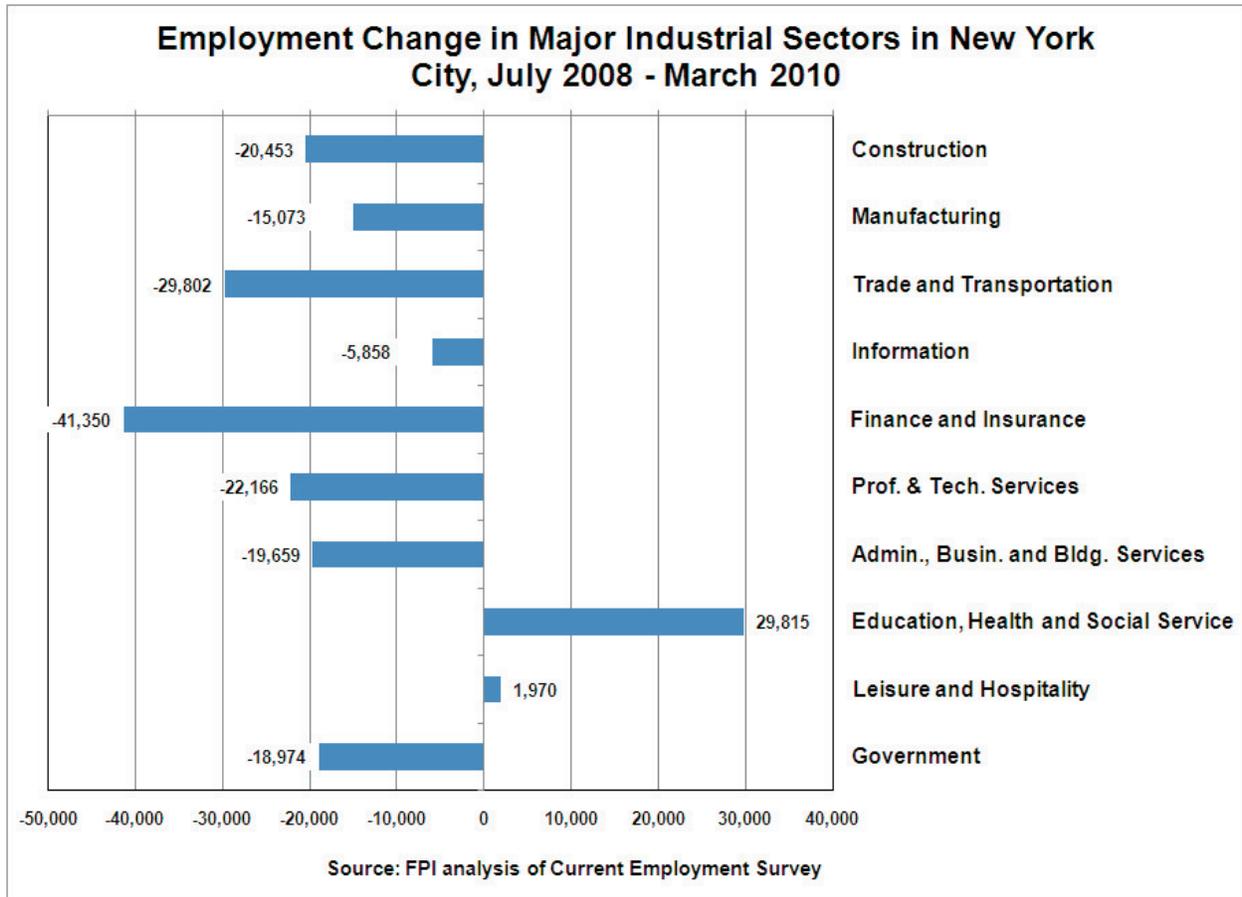


CHART 1

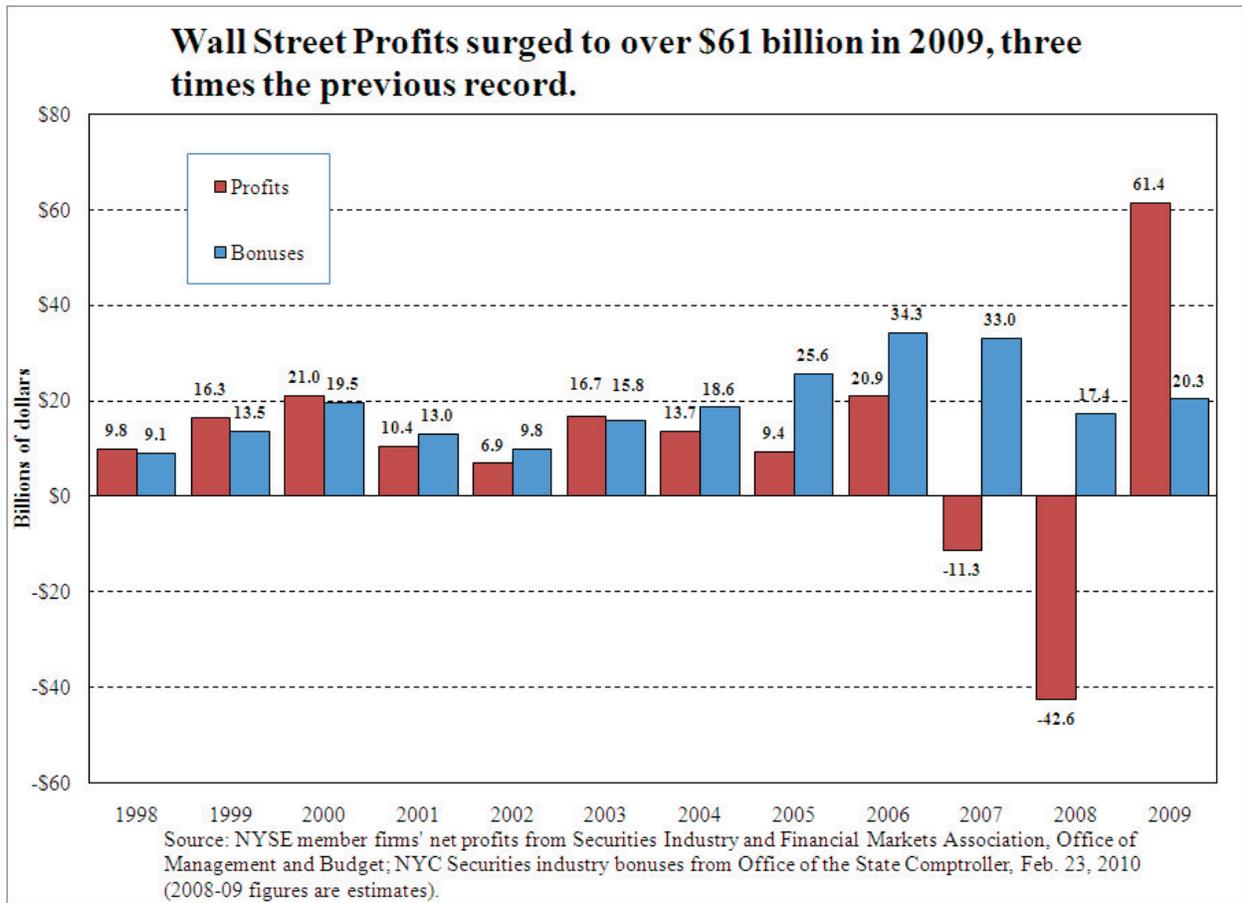


CHART 2

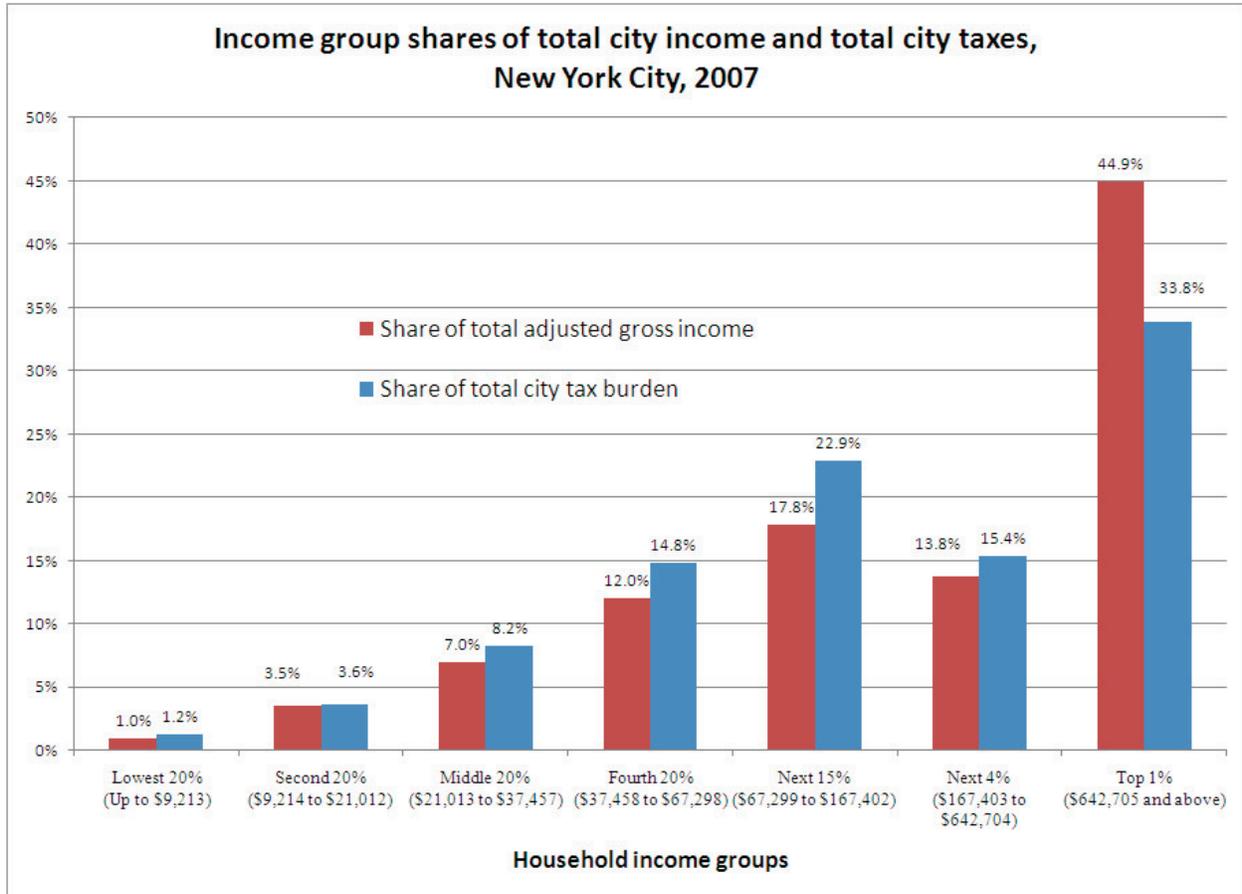


CHART 3