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February 16, 2023

Executive Summary

As we head into fiscal year 2024, with our recovery from the Covid pandemic still underway, New Yorkers face a rising cost of living and uncertainty about a potential recession. The state budget – our state fiscal policy – provides the best tools by which we can manage economic uncertainty and stabilize the quality of life and the cost of living for working New Yorkers.

Policy scholars now use the framework of "social investment" to think about strategies that stabilize the economic wellbeing of working people. While traditional models of social insurance (such as social security) are still essential pillars of welfare state policy, the idea of social investment is both broader and more dynamic. It encompasses a range of policies that proactively enhance people's capacities and opportunities, rather than just insuring economic risks. These policy models include child care and early childhood education, lifelong opportunities for education and training, active labor market policies, policies that ease the transition in and out of paid work, such as parental leave, and long-term care. If New York is going to become a state for working families, where everyone can both thrive and be comfortable, we will need to pursue a policy agenda of social investment.

Unfortunately, our recent fiscal history has moved starkly in the opposite direction. Between the financial crisis of 2008 and the Covid pandemic, New York State saw its public finances battered from all directions. The imposition of a 2 percent annual spending cap, combined with tax cuts for the wealthy and corporations, as well as rampant tax breaks for businesses, caused the state budget to grow far more slowly than the state economy. State spending declined from 7.1 percent to 5.7 percent of New York's GDP in this period. Meanwhile, the public sector workforce lost tens of thousands of jobs that have never been regained. The fiscal history of this period is presented in great detail in the last chapter of this book.

This year's Executive Budget by and large maintains the fiscal status quo. While state operating funds would grow by 2 percent, after accounting for inflation this would be a 1.4 percent decrease in total spending. The budget makes good on the Governor's promise to fully fund foundation aid, and allows normal Medicaid spending growth, but otherwise makes minimal investments in programmatic spending areas. The Governor's proposal to index the minimum wage to inflation includes too many limitations, leaving low wage workers worse off in real terms than they were before the pandemic. The proposed expansion of childcare subsidies is significantly lower than in previous years, and it fails to move towards a universal system. The proposed funding for the MTA is both short-term and fails to close the budget gap. Rather than sustained social investment, this Executive Budget seems to put its hope in tax breaks for businesses to improve the quality of life for working New Yorkers. Indeed, the Executive Budget's apparently ambitious housing agenda relies largely on tax incentives, while allowing a billion-dollar rental assistance program for low-income tenants to expire.

The chapter on tax policy presents the means by which the state could raise substantial new revenues on a sustainable basis. Options include raising the personal income tax, increasing tax rates on capital gains, taxing pass-through businesses, and conforming to a federal law that taxes multinational profit-shifting. An ambitious social policy agenda must begin by taking account of its costs, and the only feasible way to finance that vision is by looking to the principles of broad-based, progressive taxation.

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The Economic Outlook

The U.S. economic outlook for fiscal year 2024 is unusually uncertain, creating challenges for fiscal planning. Inflation, though now on a clear downward trend, remained stubbornly high through 2022. In an effort to tame inflation, the Federal Reserve repeatedly raised interest rates, slowing economic activity for the sake of lowering inflation. The central economic questions for 2023 are whether the Federal Reserve, in its attempt to constrain inflation, will send the U.S. economy into a mild recession.

Economic forecasters have coalesced around an expectation of 0.5 to 1.0 percent real GDP growth — a sharp slowdown from 1.9 percent in 2023. Forecasters' growth expectations for 2023 deteriorated consistently through 2022 as inflation remained high and, accordingly, expected interest rates have risen. While a half-point range in consensus economic forecasts is not unusually large, underlying economic uncertainty is unusually high.

In its most recent Summary of Economic Projections, the Federal Open Market Committee (FOMC, the Federal Reserve body that determines interest rates) forecast 0.4 to 1.0 percent real GDP growth. While most economic forecasters expect positive GDP in 2023, many also expect a mild recession. These projections are mutually consistent insofar as a brief recession followed by positive catch-up growth could still result in positive annual growth. In a survey of macroeconomists conducted by Financial Times and Initiative on Global Market (FT-IGM), 80 percent expected a recession in 2023. While the median projection of the Federal Reserve Bank of Philadelphia's Survey of Professional Forecasters (SPF) does not predict a recession in any quarter of 2023, it registers just 0.2 percent in the first and second quarters before regaining ground at the end of the year.

Figure 1. Selected economic forecasts for 2023

	Projected GDP growth (%)	Projected U.S. unemployment (%)
FOMC[1]	0.4 to 1.0 (0.5)	4.4 to 4.7 (4.6)
FT-IGM[2]	0.0 to 2.0 (1.0)	4.0 to 5.5 (4.5)
SPF[3]	0.7	4.4
New York State Quick Start[4]	0.5 to 1.1 (0.7)	–
FY24 Executive Budget	0.5	4.3
IMF–Oct 2022	1.0	–
IMF–Jan 2023	1.4	–

Median in parentheses. FOMC range represents midrange estimates; IGM range represents 10th and 90th percentiles. Unemployment projections are for the fourth quarter.

Economic forecasters generally see the U.S. unemployment rate rising from its current 3.7 percent to the mid-four percent range. While 4.5 percent unemployment would be historically low for a recession, as with GDP projections, it may be consistent with recession. The pace at which unemployment rises has historically acted as an indicator of recession. According to the Sahm Rule, a half percentage point increase in unemployment has been a reliable early indicator of past recessions.[5]

New York's fiscal year 2024 executive budget makes conservative projections within the range of other forecasters. The budget expects 0.5 percent GDP growth and 4.3 percent unemployment in 2023. The budget's GDP estimate falls at the bottom of the range of estimates made during the state's quick start process, in which the state's executive office, legislature, and comptroller contribute economic and fiscal forecasts.

The state's Division of Budget prudently uses conservative economic projections to minimize downside fiscal risks. The most recent economic data, however, shows continued unwinding of price and wage inflation and amid continued labor market resilience. These indicators appear to be consistent with a "soft landing" in which inflation returns to its two percent target without heightened interest rates triggering a recession.[6] In January 2023, the International Monetary Fund (IMF) revised its 2023 growth estimate for the U.S. upward. After consistent downward revisions through 2022, the IMF now expects U.S. real GDP to increase 1.4 percent, up from the 1.0 percent estimate made in its October economic outlook.[7]

Importantly, DOB's economic pessimism extends well past 2023. The agency revised its economic expectations for both the U.S. and New York State downward not just for 2023, but for each outyear as well. In its fiscal year 2023 economic outlook, DOB expected real GDP growth of 2.3 percent and 2.4 percent in 2024 and 2025, respectively. This year, DOB marked these projections down to 1.7 percent and 2.3 percent, respectively. Expected personal income growth was similarly revised down.[8] While apparently minor, changes to these forecasts can affect significant revisions to future revenue projections.

It is almost certain that in 2023 economic growth will slow and unemployment will rise. Whether the slowing economy will avoid a recession remains unclear. For state policymakers, the formal declaration of a recession in the U.S. matters less than the timing and severity of fiscal and economic downturns. Policymakers face the balancing act of conservatively budgeting revenue projections to ensure spending can be covered in a downturn while ensuring investments are sufficient to provide services for the New Yorkers who will bear the brunt of a downturn.

If New York does face a mild recession, it will be particularly important to increase investments in essential public services and income supports. The experiences of the last two recessions demonstrate that retrenching in the midst of a crisis, as happened after 2008, exacerbates downturns; conversely, safety net supports such as the stimulus payments made during the COVID-19 pandemic accelerate the economic recovery from a recession and provide fiscal stability for households most at risk from economic downturns.

New York's Economic Recovery from the Covid Pandemic

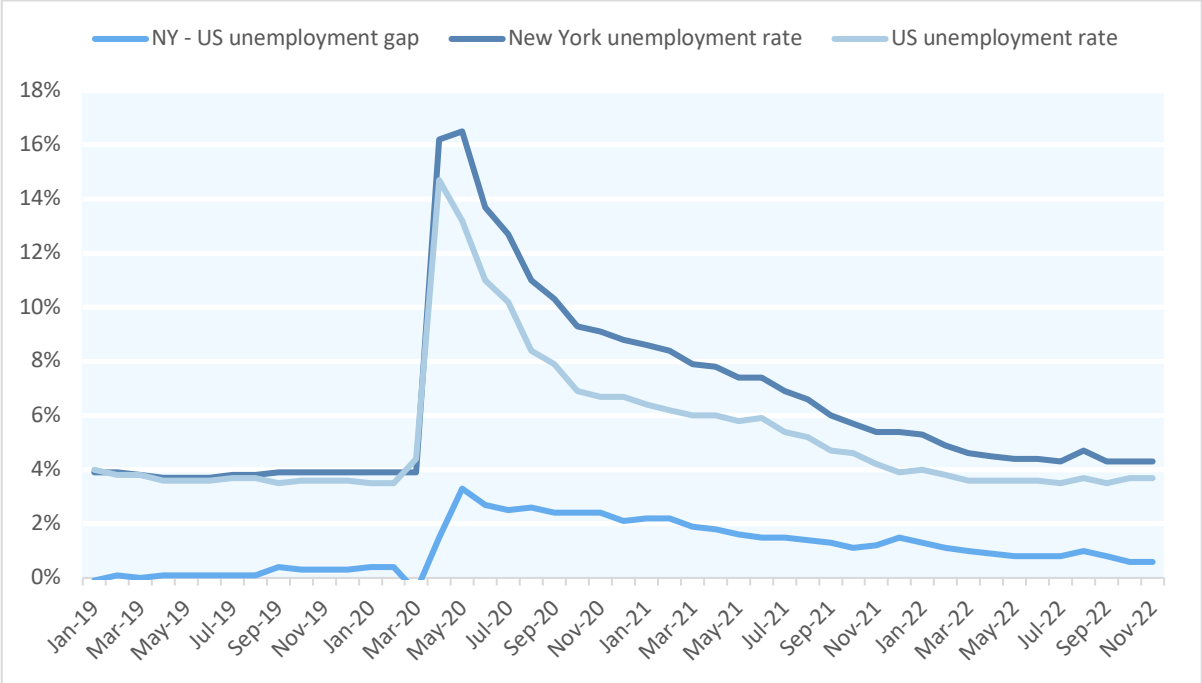
New York's economic recovery from Covid continued at a brisk pace in 2022. However, the state was hit harder by the initial phase of the pandemic than the rest of the country. Despite the state's recent

improvement across a range of economic indicators, including unemployment and job growth, many of these indicators remain below their pre-pandemic levels. For this reason, the state enters the elevated economic uncertainty of 2023 on more precarious economic footing than much of the rest of the U.S.

The recession caused by the Covid pandemic was far more intense than past recessions, but also shorter lived. The first major epicenter in the U.S., New York suffered devastating loss of life in the first months of the pandemic. Between February 2020 and April 2020, the state lost nearly two million jobs, a 20.2 percent drop. For the U.S. overall, 14.4 percent of jobs were lost in the Covid recession. The number of active claims for unemployment insurance in the state rose from 167 thousand immediately before the March lockdowns to 2.2 million in May 2020. New York's unemployment rate reached a peak of 16.5 percent in May 2020, nearly two percentage points higher than the U.S. rate. By the end of 2020, unemployment was more than halfway back to pre-pandemic levels. The state economy continues to add jobs, but the pace of employment recovery has been uneven across the state and sectors of its economy.

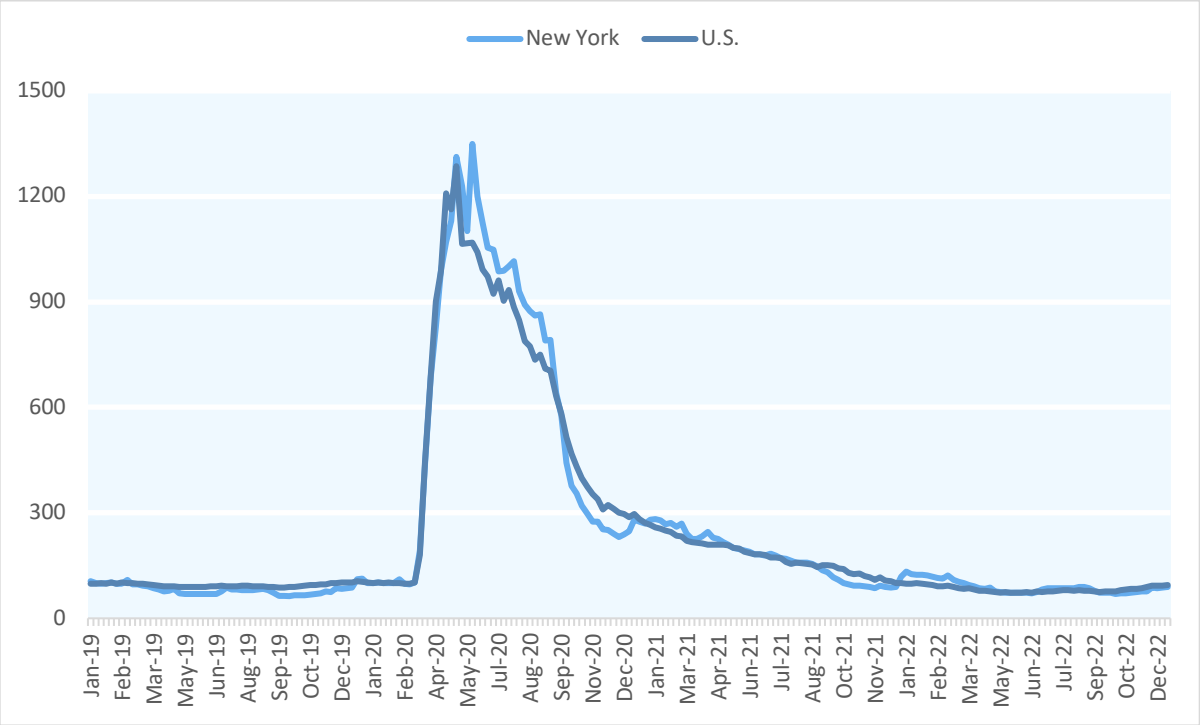
Unemployment

Figure 2. NY vs US Unemployment, 2019-2022



New York's unemployment was on par with the U.S. unemployment rate through 2019. After rising from 3.9 to 16.5 percent between March and May 2020, New York's unemployment rate began falling quickly. The state's unemployment rate was 8.8 percent by the end of 2020, and fell to 4.3 percent in July 2022, a level at which it has since generally remained. Since July 2022, the U.S. unemployment rate has oscillated around 3.6 percent — 0.7 percentage points below the New York rate. This differential is driven by New York City's persistently elevated unemployment rate, which stood at 5.9 percent in December 2022. Excluding the city, the state's unemployment would be 3.2 percent.[9]

Figure 3. New York and U.S. continuing UI claims, indexed to February 2020



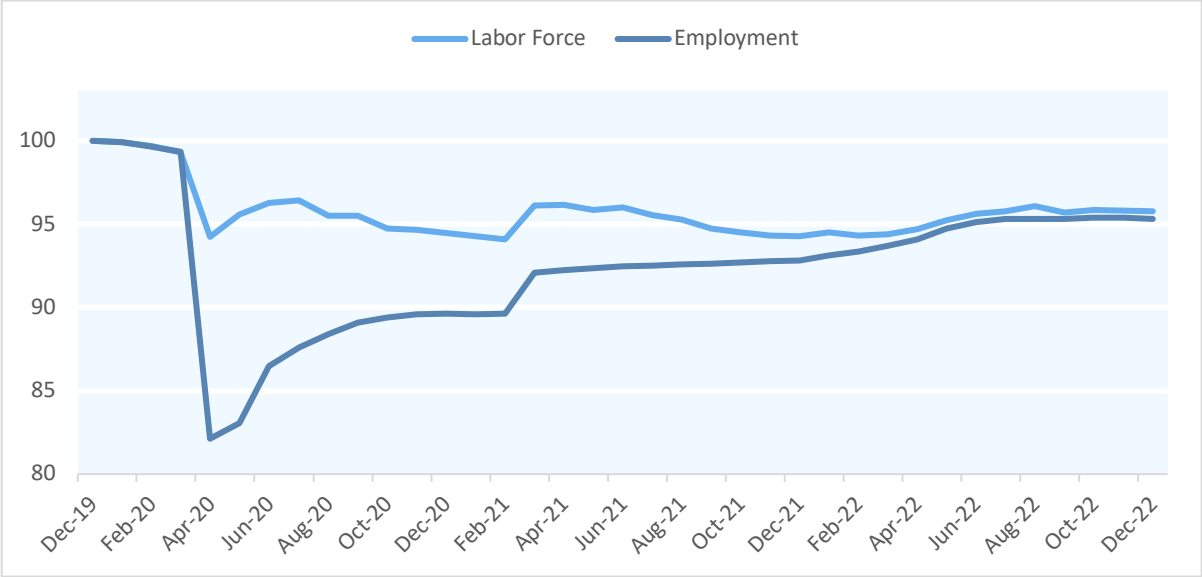
New York workers' continuing claims for unemployment insurance (UI) benefits — the number of all weekly recipients of UI payments — has more closely tracked the U.S. through the crisis. The number of continuing claims in New York rose 13-fold to 2.2 million between the second week of March 2020 and the final week of May 2020. New York and U.S. UI claims both returned to pre-pandemic levels by the end of 2021 and have since remained lower.

New York's Labor Force

The New York labor force has been slower to recover than the unemployment rate. The Covid recession appears to have reduced the size of the U.S. labor force — the sum of employed and unemployed workers — relative to its pre-pandemic trajectory in part by accelerating retirement for many workers.[10] In doing so, Covid lowered the total number of jobs in the economy even as unemployment fell to historic lows. The same pattern is especially evident in New York. Despite the unemployment rate having returned to its pre-pandemic level, the total labor force was 4.5 percent smaller than its pre-pandemic level, as of December 2022.

As unemployment rose and remained elevated, the number of employed New York residents followed a sharper downward trajectory than its labor force. By December 2020, New York employment was 10.2 percent lower than its level in December 2019. In 2021 employment grew by 4.1 percent, followed by 1.9 percent growth in 2022. As of December 2022, the most recent data available, employment remained 4.8 percent below its 2019. The near parity with the decline in labor force reflects the normalization of the unemployment rate.[11]

Fig. 4. New York labor force and employment as percentage of 2019 level

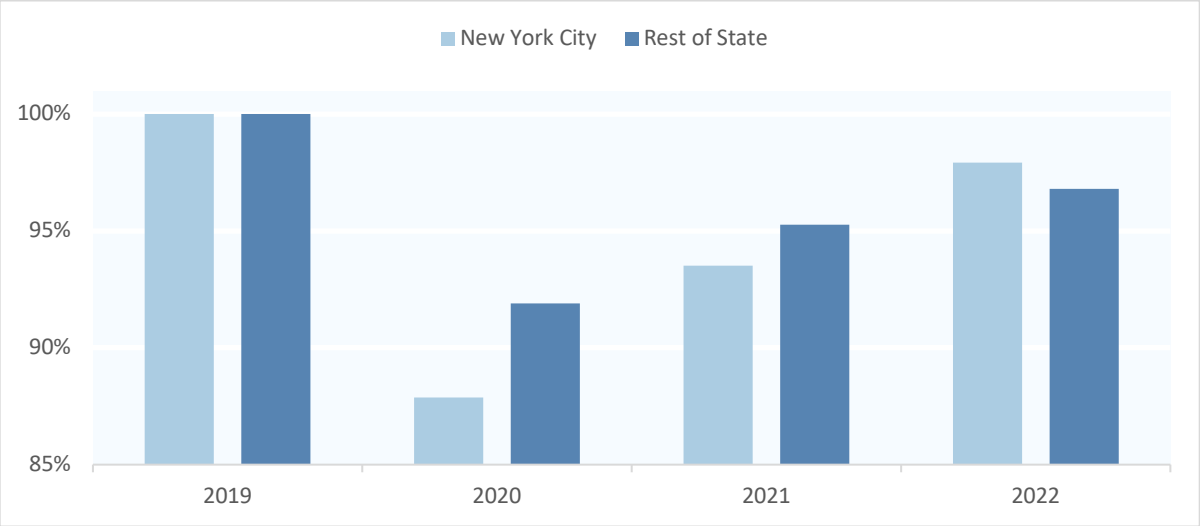


Job Growth

The number of jobs based in New York (reported by place of employment, rather than place of worker residence) provides another economic indicator that better reflects the state's economic and fiscal base. This measure of job growth finds greater improvement for the state economy than the labor force indicators. The data finds New York-based jobs fell by the same amount as New York resident employment — down 10.0 percent between December 2019 and December 2020. However, the ensuing job growth recovery has been faster, rising by 5.0 percent in 2021 and 3.1 percent in 2022. As of December 2022, the most recent data available, the state's jobs were 2.7 percent below 2019 levels.

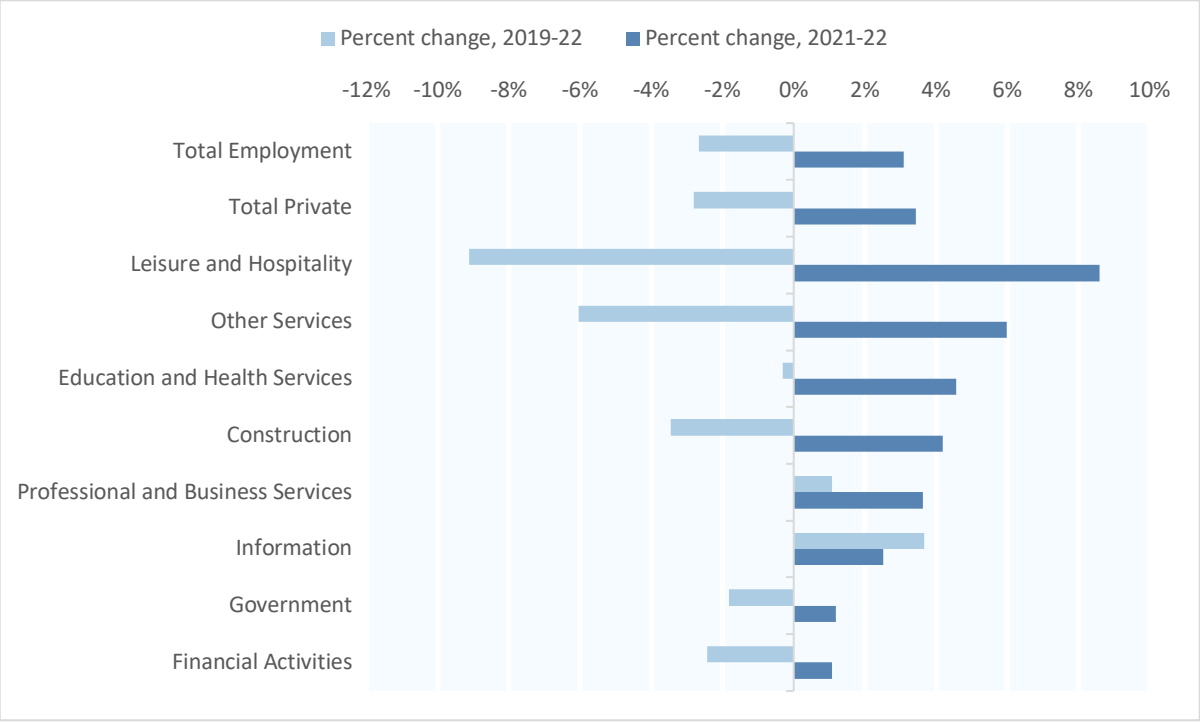
New York City is a major driver of the state's strong job growth relative to its lagging labor force recovery. While the city's total jobs fell further than the rest of the state in 2020, it has since rebounded faster. The city's total December 2022 jobs were just 2.1 percent short of 2019 levels, compared with 3.2 percent in the rest of the state.

Figure 5. Total jobs in New York City and the rest of the state as percentage of 2019 level



No sector of New York's economy was hit harder than its tourism-driven Leisure and Hospitality industry. Employment in the sector fell by 37.6 between December 2019 and December 2020, a loss of 356.4 thousand jobs. Despite growing 8.6 percent in 2022 — the fastest of any sector — employment remains 9.1 percent below pre-pandemic levels, the lowest of any sector. As of December 2022, two sectors had surpassed pre-pandemic levels: Professional and Business Services, which includes white collar businesses such as law and accounting, and Information, which includes media, software, and communications technology businesses. The recovery of these relatively high-wage sectors has played a role in the rebound of the state's personal income tax revenue, despite lower overall employment.

Figure 6. New York employment, percent change from 2019 and 2021 by industry



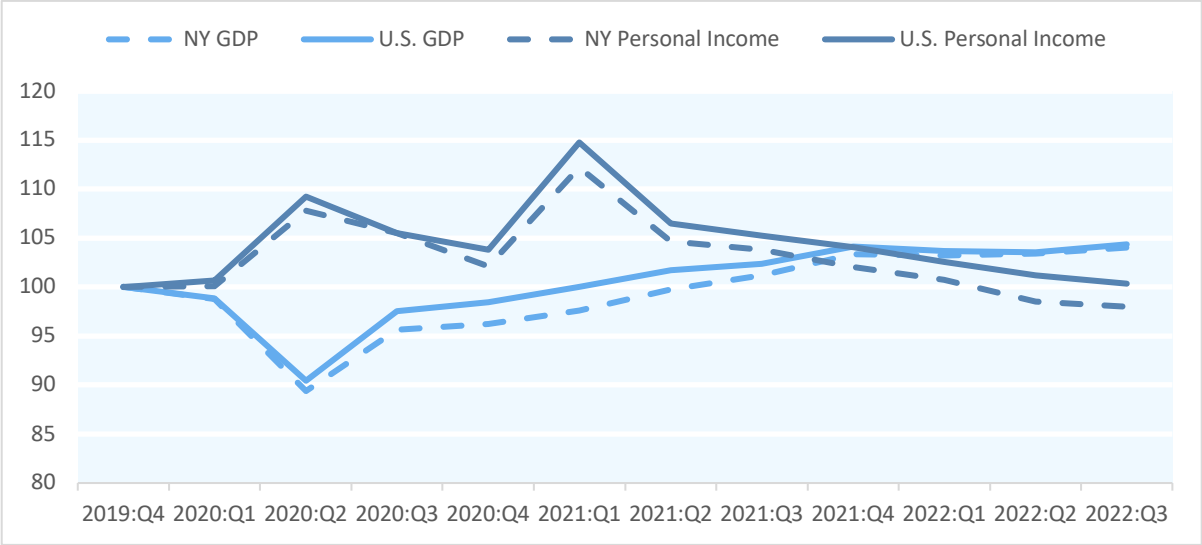
Economic Growth

Unlike employment, New York's total economic output — as measured by the state's real gross domestic product (GDP) — quickly rebounded to its pre-Covid level. After falling 10.6 percent between the fourth quarter of 2019 and the second quarter of 2020, the state's GDP passed its pre-Covid level in the third quarter of 2021. The state's economy continued its expansion, exceeding pre-Covid peak by 4.0 percent in the third quarter of 2022, the most recent data available. While New York's GDP fell further than that of the U.S. as a whole in 2020, its current level is on par with national economic growth.

By contrast, elevated inflation in 2021 and 2022 held down real personal income growth in both New York and the U.S. While federal pandemic relief – channeled through a variety of programs, including direct stimulus payments and enhanced UI benefits – lifted income in 2020 and 2021, inflation pulled real income back to pre-Covid levels by the end of 2021. As of the third quarter of 2022, U.S. incomes were on par with the fourth quarter of 2019, after adjusting for inflation, while New York incomes were 2.0 percent lower.

Figure 7. New York and U.S. real GDP and personal income growth

Indexed to the fourth quarter of 2019



A further gauge of New York's economic recovery is provided by the index of coincident economic indicators compiled by the state's Department of Labor. The index, which is designed as a leading indicator of the state's economy, is a composite measuring wages, employment, consumer spending, and manufacturing activity. As of December 2022, the most recent data available, the index remains 3.0 percent short of its December 2019 level. This post-Covid high follows 6.4 percent growth in 2021 and 3.4 percent growth in 2022. As reflected in other measures, brisk growth in the 2021 and the first half of 2022 slowed considerably — but remained positive — in the second half of the year.

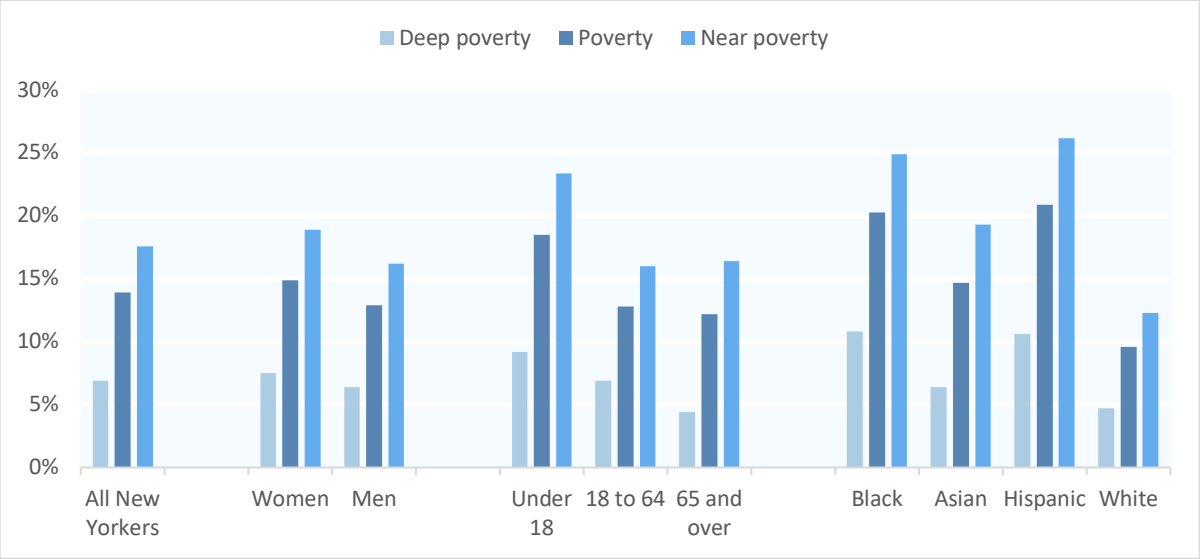
Poverty

After falling to a historically low 12.7 percent in 2020 — driven by unprecedented federal relief funding — poverty in New York ticked up in 2021, the most recent year for which data is available. With stimulus

programs winding down in 2021, the state's poverty rate rose to 13.9 percent, 0.8 percentage points higher than 2019. By comparison, the U.S. poverty rate rose from 11.9 percent in 2020 to 12.8 percent in 2021.[12]

Poverty varies considerably across demographic groups. In 2021, 6.9 percent of New Yorkers lived in deep poverty in 2021, with incomes less than half of the federal poverty level (itself an inadequate gauge of economic hardship).[13] This rate was higher for Black and Hispanic New Yorkers as well as those under age 18, who experienced deep poverty at rates of 10.8 percent, 10.6 percent, and 9.2 percent, respectively. These trends held across poverty levels, with economic hardship disproportionately affecting women, children, and Black, Hispanic, and Asian New Yorkers. Nearly one-quarter of children (23.4 percent) and Black New Yorkers (24.9) and more than one-quarter of Hispanic New Yorkers (26.2 percent) experienced near poverty in 2021, with incomes less than 125 percent of the federal poverty level.[14]

Figure 8. Poverty level by selected characteristics, 2021



Population Trends

New York State's total population was hit hard by Covid. After more than a decade of continued population growth, the state population has fallen every year since 2020.[15] Population losses have been led by net domestic outflow — New Yorkers leaving for other states in excess of residents of other U.S. states moving into New York. However, net domestic outflow is not new to New York. A major port of entry to the U.S., New York has long attracted international immigration, as well as younger Americans, while sending residents, on net, to the rest of the country. This model has historically been consistent with sustained population growth and economic dynamism. For this reason, a deeper analysis of the state's population dynamics and their relationship with its fiscal and economic structures is necessary to provide full context for current trends.

The most recent U.S. Census Bureau population estimates find that the state's population fell by 180,000 to 19.7 million between 2021 and 2022.[16] This loss was lower than the decline of 251,000 in 2021, but remains above 2020's decline of 93,000 and sets NY's population back after a decade of sustained population growth prior to the Covid pandemic.

After having been depressed in 2020 and 2021, international immigration returned to its highest level since 2016, with a net gain of 78,000 residents in 2022. Natural population growth (the number by which births outnumber deaths) also ticked up, adding 36,000 to the state population. New York outpaced the national median on both these measures. Still, domestic out-migration remains elevated, with net outflow estimated at 296,000 in 2021 and 300,000 in 2022.

New York's economic geography contributes to its longstanding net domestic outflow. That consistent net domestic outflow has coincided with sustained population and economic growth provides crucial context for the state's population dynamics. Net domestic migration is not straightforwardly predictive of economic dynamism — the relationship between the two is far more complex.

Cities are home to the nation's highest-productivity and highest-value economic sectors. At the same time, urban centers in the U.S. tend to experience sustained net domestic outflows. This is true of cities in the Northeast and California as well as sunbelt states like Florida and Texas. While this trend has accelerated in recent years, a continuous flow of Americans from cities to the suburbs predated the Covid pandemic.[17] Nevertheless, the populations of large U.S. cities, including New York City, have generally continued to grow, their populations driven by births outnumbering deaths and by immigration from abroad. This dynamic is possible even in a demographically static city. If two adults move into a city, start a family, and decamp for the suburbs as a family of four, outflow (4 people moved out) will have doubled inflow (2 people moved in) despite no lasting change to the city's demographic composition.

New York is particularly exposed to this dynamic due to the urban concentration of its population: Nearly two-thirds (65 percent) of the state's population lives in the New York metropolitan area. Because the state's labor markets outside the New York metropolitan area are generally weaker, downstate population growth necessarily sets the pace of the state's growth. However, 62 percent of the metropolitan area's suburbs — the expected relative recipients of net in-migration from the city — are not in New York State.[18]

Compounding this dynamic, New York's downstate suburbs build far less housing than those in New Jersey and Connecticut.[19] This positions New York State for sustained net domestic outflow even as the metropolitan area continues to create jobs and attract residents. While county-level 2022 estimates will not be released until March 2023, 2021 estimates found that migration out of New York City accounted for nearly all (97 percent) of the state's net domestic outflow, with slight net outflow in downstate suburban counties and population growth limited to the Hudson Valley and Capital District.

Evidence from the Internal Revenue Service's migration data illustrates this dynamic. In 2020, the most recent year for which data are available, New York's highest net domestic outflow went to two counties closest to New York City: Hudson County, New Jersey and Fairfield County, Connecticut. Nearly one-third of New York's net out-migration flowed to the neighboring states of New Jersey, Connecticut, and Pennsylvania. California and Florida rounded out the top five states receiving New Yorkers on net.[20]

The cost of housing likely drives these migration patterns. Housing costs are the largest single expenditure for the average U.S. household.[21] New York City and its in-state suburbs tend to have far higher housing costs than out-of-state suburban counties, or other top destinations for outbound New Yorkers. Of the top twenty largest county-to-county flows out of New York State, median housing costs were substantially lower in the destination county. (Note that migration data is available on a county-to-county basis). On

average, annual mortgage costs for median-priced homes are $18,300 lower in destination counties — a savings of 34 percent — than in New York origin counties. In six of the twenty county-to-county pairs, median home prices in the New York origin county were twice as high as in the destination county. New York housing costs were higher than destination costs for all groups except Bronx residents heading to Fairfield County, Connecticut or Bergen County, New Jersey. Three other major New York suburban counties — Rockland, Nassau, and Suffolk — have higher median home prices than all neighboring out-of-state suburbs (even though these counties are not in the top twenty county-to-county migration pairs).[22]

As most New York City households are renters, New York's high rents also play a significant role driving households towards the suburbs. Of the top twenty county-to-county moves out of New York, renters are likely to reap savings in all but two.[23] On average, rents are $5,600, or 19 percent, lower in destination counties than in their respective New York origin counties.

Differences in housing costs for New York's out-migrants far exceed prospective savings on state and local taxes. Across all twenty county-to-county pairs, median income families leaving New York can expect average annual tax savings of $1,200 — 15 times less than they might save on mortgage costs and five times less than potential rent savings. In other words, the typical family that moves out of New York State saves 15 times more from lower housing costs than they do from lower taxes. Mortgage cost savings were at least eight times higher than tax savings in 16 of the 20 county-to-county pairs.[24] For households moving for economic reasons, cost differentials for their largest single expenditure — housing — vastly exceed any potential tax savings.

Figure 9. Estimated annual housing and tax savings for a middle-income household for the top twenty county-to-county migration flows from New York State

From	To	Mortgage savings	Rent savings	Tax savings
Manhattan	Hudson County, NJ	$36,622	$6,444	$729
Manhattan	Fairfield County, CT	$37,819	$8,664	$1,184
Westchester	Fairfield County, CT	$10,390		$1,184
Manhattan	Los Angeles County, CA	$24,039	$9,060	$1,647
Manhattan	Bergen County, NJ	$34,949	$8,928	$729
Brooklyn	Essex County, NJ	$15,524	$4,812	$729
Brooklyn	Hudson County, NJ	$14,274	$ (1,692)	$729
Brooklyn	Los Angeles County, CA	$1,692	$924	$1,647
Queens	Bergen County, NJ	$6,038		$729

Queens	Hudson County, NJ	$7,710		$729
Manhattan	Miami-Dade County, FL	$41,141	$7,860	$5,071
Manhattan	Essex County, NJ	$37,871	$12,948	$729
Bronx	Fairfield County, CT	$(2,740)		$1,184
Brooklyn	Ocean County, NJ	$19,766		$729
Staten Island	Monmouth County, NJ	$1,561		$729
Brooklyn	Philadelphia County, PA	$30,987	$9,156	$2,900
Brooklyn	Fairfield County, CT	$15,472	$528	$1,184
Brooklyn	Union County, NJ	$17,719	$5,424	$729
Brooklyn	Middlesex County, NJ	$20,233	($576)	$729
Bronx	Bergen County, NJ	$(5,610)		$729

FPI estimated potential annual savings for a median income family's mortgage costs, rent costs, and taxes for all counties included in the top twenty county-to-county migration flows. FPI estimates of mortgage costs used data on median-priced homes by county from Zillow to estimate annual payments on a 30-year fixed rate mortgage at 3.5 percent (the average rate over the period in question; mortgage cost differentials would be much greater under current rates). Rent costs were estimated as the annual median market rents by county using data from ApartmentList. Tax data are only available at the state level. Tax savings were estimated as the state-to-state difference in annual state and local tax liabilities for each county pair using state and local tax data estimated by the New York State Division on Budget.[25]

Methodological Note: Annual Census Population Estimates

The Census' undercount of New York accounted for 41 percent of the difference between annual estimates and the ten-year 2020 census count for the entire U.S.

Every ten years, the U.S. Census Bureau undertakes a complete count of the U.S. population. This count, the decennial census, is based on a survey of every address in the U.S. and serves as the base for the Bureau's annual population estimates over the following decade. Annual estimates, or intercensal estimates, use administrative data on births, deaths, and net international migration to estimate population change since the national decennial count.

State-level population estimates further account for net domestic migration, and are adjusted to collectively equal the national annual estimates. Every set of annual intercensal estimates include population totals for each year between the current year and the most recent decennial census. These sets of estimates, called vintages, include updated data and consistent methodology, and supersede estimates included in previous vintages.[26]

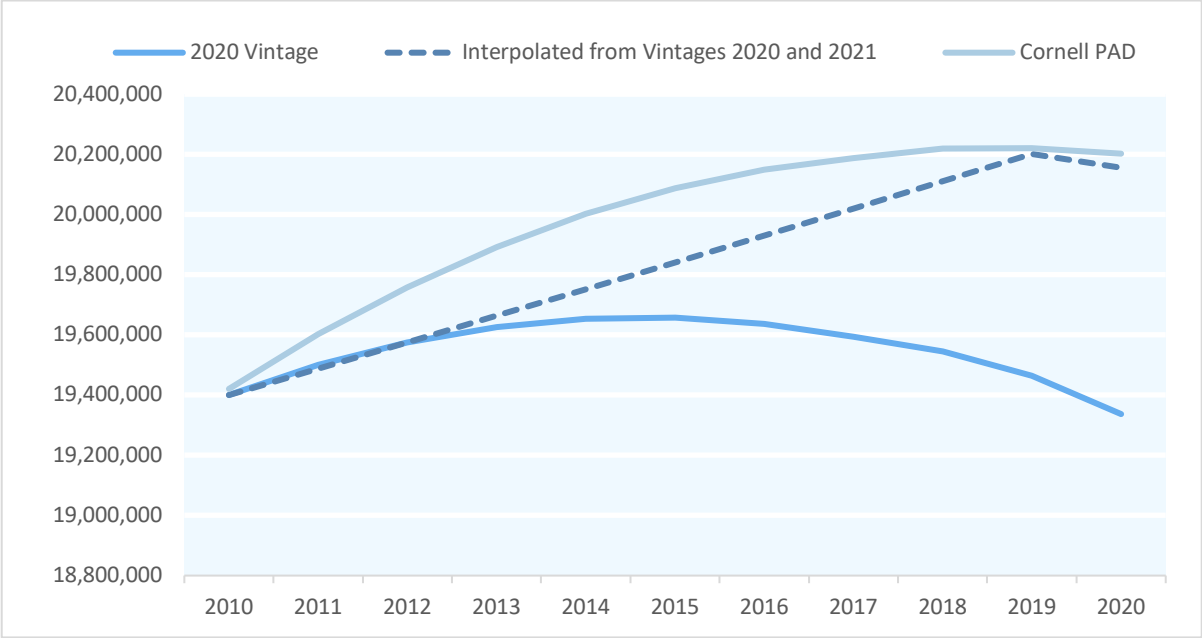
The Covid pandemic caused significant challenges for Census population estimates. Lags in the availability of administrative data and delays processing decennial census data required adjustments to the 2020 population base used by the 2021 and 2022 vintages. As with pre-pandemic population estimates, the most recent intercensal estimates use the 2020 decennial census as its base count for the total population. However, post-pandemic vintages have supplemented the 2020 decennial census with vintage 2020 estimates – the final intercensal estimates that use the 2010 decennial as a population base — and the 2020 demographic analysis to form a "blended base" that allows the Bureau to estimate demographic variables within the total population.[27]

Census methodology is unusually consequential for New York State. Vintage 2020 intercensal estimates showed New York's population peaking at 19.7 million in 2015, then falling continuously to 19.3 million in 2020 — below the 2010 base population of 19.4 million. This turned out to be a dramatic undercount of the state's population. The 2020 decennial census recorded New York's actual population in 2020 to be 20.2 million — 4.2 percent higher than the intercensal estimate. As a percentage of population, the intercensal undercount of New York was the second-highest in the U.S., behind New Jersey. In absolute terms, New York's undercount accounted for 41 percent of the difference between the intercensal and decennial 2020 estimates for the entire U.S.[28] New York City's efforts to add missing housing units to the Census Bureau's list of addresses appears to have played a significant role in the 2020 decennial count.[29]

That New York State experienced four percent growth over the 2010s rather than population loss has substantial bearing on public policy. Regional population loss stemming from a weak labor market, for instance, would require a different policy intervention than population stagnation amid a constrained housing supply. The lack of quality data on population dynamics impedes such diagnoses and responses.

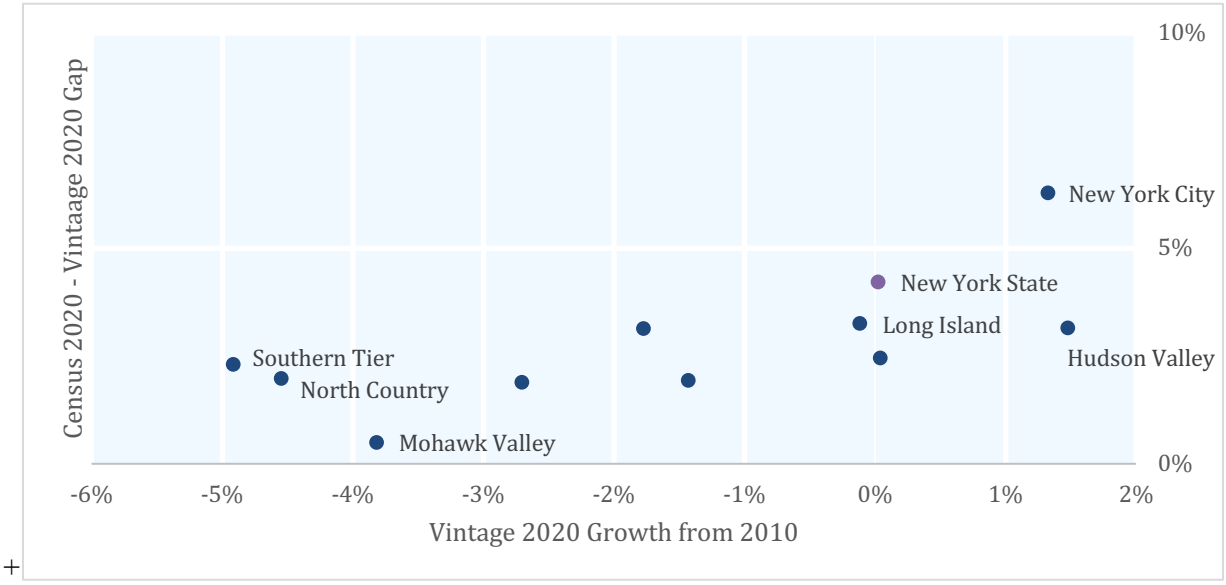
In Summer 2023, the Census Bureau will release population estimates for the 2010s that are consistent with the 2020 decennial.[30] In the interim, the Cornell Program on Applied Demographics (PAD) has constructed intercensal estimates for 2010 to 2020. PAD estimates provide valuable insight into the state's population over the last decade. Prior to the 2020 decennial, it appeared that New York City's population was declining since 2016. It now appears likely that the city continued to grow until the pandemic. By contrast, regions of Upstate New York outside of the Hudson Valley and Capital Region likely experienced near-continuous population loss through the decade.[31]

Figure 10. New York 2020 population estimates from Vintages 2020 and 2021 and Cornell PAD



Further, intercensal estimation errors may be greater in faster-growing regions of the state. Intercensal estimates showed New York City grew 1.3 percent over the decade, the second-fastest growth in the state. Decennial estimates marked the city's growth up by 6.3 percentage points — the largest revision in the state — to 7.7 percent. By contrast, slow growing regions, like the Mohawk Valley, tended to see only minor upward revisions in the decennial census.

Figure 11. Regional growth in intercensal estimates, 2010 to 2020, and gap between 2020 intercensal and decennial estimates



Covid-related disruptions to census methodology continue to impede pre-pandemic processes. Those processes themselves provided a misleading picture of the state's population dynamics over the last decade.

While intercensal estimates provide valuable information of population change in the state, policymakers, researchers, and the general public should remain aware that the estimates are subject to significant revision in subsequent vintages and that different vintages are not comparable with each other. A more complete analysis of the state's social conditions requires carefully contextualizing census population estimates and consideration of a wider range of social and economic indicators.

[1] Board of Governors of the Federal Reserve System, *Summary of Economic Projections, December 14, 2022* (December 2022), https://www.federalreserve.gov/monetarypolicy/files/fomcprojtabl20221214.pdf.

[2] Financial Times-Chicago Booth Initiative on Global Markets, *US Marcoeconomists Survey* (December 2022), https://www.igmchicago.org/wp-content/uploads/2022/12/RESULTS-2022-12-02-Survey-07.pdf.

[3] Federal Reserve Bank of Philadelphia, *Fourth Quarter 2022 Survey of Professional Forecasters* (November 2022), https://www.philadelphiafed.org/surveys-and-data/real-time-data-research/spf-q4-2022.

[4] New York State Division of the Budget, *2022 Joint Report on Receipts and Disbursements* (November 2022), https://www.budget.ny.gov/pubs/press/2022/fy24-quickstart/report-fy24-quickstart.pdf.

[5] The Sahm Rule specifies that a 0.5 percent increase in the three-month moving average unemployment relative to lows from the past 12 months likely indicates recession.

[6] James Politi and Colby Smith, "No signs of US slowdown in surprisingly robust jobs market" *Financial Times* (February 2023), https://www.ft.com/content/cb2d25a3-456e-4cd7-bb27-484fe9776340.

[7] International Monetary Fund, *World Economic Outlook Update: Inflation Peaking amid Low Growth: January 2023* (January 2023), https://www.imf.org/en/Publications/WEO/Issues/2023/01/31/world-economic-outlook-update-january-2023 and October 2022 edition.

[8] New York State Division of the Budget, *Fiscal Year 2024 Executive Budget Economic and Revenue Outlook* (February 2022), https://www.budget.ny.gov/pubs/archive/fy24/ex/ero/fy24ero.pdf and fiscal year 2023 edition.

[9] New York State Department of Labor, "NYS Economy added 22,100 private sector jobs in December 2022"

(January 2023), https://dol.ny.gov/system/files/documents/2023/01/nys-economy-added-22100-private-sector-jobs-in-december-2022.pdf.

[10] Jeanna Smialek and Ben Casselman, "Retirees are One Reason the Fed has Given Up on a Big Worker Rebound" *New York Times* (December 2022), https://www.nytimes.com/2022/12/27/business/economy/labor-shortage-retirees-boomers.html.

[11] Bureau of Labor Statistics, "State and Metro Area Employment, Hours, and Earnings" (accessed January 2023), https://www.bls.gov/sae/data/.

[12] U.S. Census Bureau, "Small Area Income and Poverty Estimates" (accessed January 2023), https://www.census.gov/data-tools/demo/saipe/#/?s_state=36&s_county=&s_district=&s_geography=us.

[13] FPWA, *Measuring Poverty and the True Cost of Living in the U.S.* (September 2022), https://www.fpwa.org/wp-content/uploads/2022/09/MEASURING-POVERTY-AND-THE-TRUE-COST-OF-LIVING-IN-THE-U.S._2022.pdf.

[14] U.S. Census Bureau, "American Community Survey Table S1703, 2021, 1-year file" (accessed January 2023), data.census.gov.

[15] While annual population estimates prior to 2020 showed population losses for New York State, these estimates have been superseded by subsequent estimates. See "annual Census population estimates" section below for a detailed discussion.

[16] Annual population estimates estimate the population as of July 1 of each year.

[17] William H. Frey, "New census data shows a huge spike in movement out of big metro areas during the pandemic (Brookings, April 2022), https://www.brookings.edu/blog/the-avenue/2022/04/14/new-census-data-shows-a-huge-spike-in-movement-out-of-big-metro-areas-during-the-pandemic/.

[18] U.S. Census Bureau "2020-2021 county population totals," (March 2022) https://www.census.gov/data/tables/time-series/demo/popest/2020s-counties-total.html. The New York metropolitan area includes counties in southern New York, northern New Jersey and Pike county, Pennsylvania. It does not include counties in Connecticut.

[19] New York City Department of Planning, "NYC Metro 2020 housing production snapshot" (November 2021), https://www.nyc.gov/assets/planning/download/pdf/planning-level/region/nyc-metro-housing-production-2020-snapshot-1121.pdf.

[20] Internal Revenue Service, "2019-2020 Migration data by individual state–New York" (May 2022), https://www.irs.gov/statistics/soi-tax-stats-migration-data-2019-2020.

[21] See Table 1: U.S. Bureau of Labor Statistics, "Consumer price index new release" (November 2022), https://www.bls.gov/news.release/archives/cpi_12132022.htm.

[22] Data from Zillow, "Zillow Home Value Index–all homes" (November 2022), https://www.zillow.com/research/data/. Housing costs are estimated as mortgage payments for median-priced home, assuming 10 percent down payment and a 3.5 percent interest rate on a 30-year fixed rate mortgage (average for the 2019-2020 data reference period).

[23] Data from ApartmentList, "current month summary" (December 2022), https://www.apartmentlist.com/research/category/data-rent-estimates. Data is incomplete because unlike home prices, which are matters of public record, rent data is based on either surveys or collected from real estate brokerages. ApartmentList estimates median market rate rents (estimated by looking at rent paid by recent movers) using data from the American Community Survey. For some markets, the sample size may be too small to generate reliable estimates.

[24] Tax liability calculated for median income New York family ($85,806; U.S. Census Bureau American Community Survey "Table S1903–2021 1-year estimates," data.census.gov. Tax data from table 6b in New York State Division of Budget "Fiscal Year 2023 Executive Budget Economic and Revenue Outlook" (January 2022), https://www.budget.ny.gov/pubs/archive/fy23/ex/ero/fy23ero.pdf.

[25] Sources: tax data from table 6b in New York State Division of Budget "Fiscal Year 2023 Executive Budget Economic and Revenue Outlook" (January 2022), https://www.budget.ny.gov/pubs/archive/fy23/ex/ero/fy23ero.pdf; rent data from ApartmentList, "current month summary" (December 2022), https://www.apartmentlist.com/research/category/data-rent-estimates; home price data from Zillow, "Zillow Home Value Index–all homes" (November 2022), https://www.zillow.com/research/data/.

[26] For more detail on intercensal population estimates, see U.S. Census Bureau, "Methodology for the United States Population Estimates: Vintage 2021" (December 2021), www2.census.gov/programs-surveys/popest/technical-documentation/methodology/2020-2021/methods-statement-v2021.pdf.

[27] For more detail on the blended base, see U.S. Census Bureau, "Briefing on the Base Evaluation and Research Team" (Fall 2022), www2.census.gov/about/partners/cac/sac/meetings/2022-09/presentation-briefing-on-base-evaluation-and-research-team.pdf.

[28] Vintage 2020 and Vintage 2021

[29] New York City Department of City Planning, "Laying the Foundation for an Accurate 2020 Census in NYC" (August 2021), storymaps.arcgis.com/stories/47d5aee928374e1aa23d85ca34ac3d78.

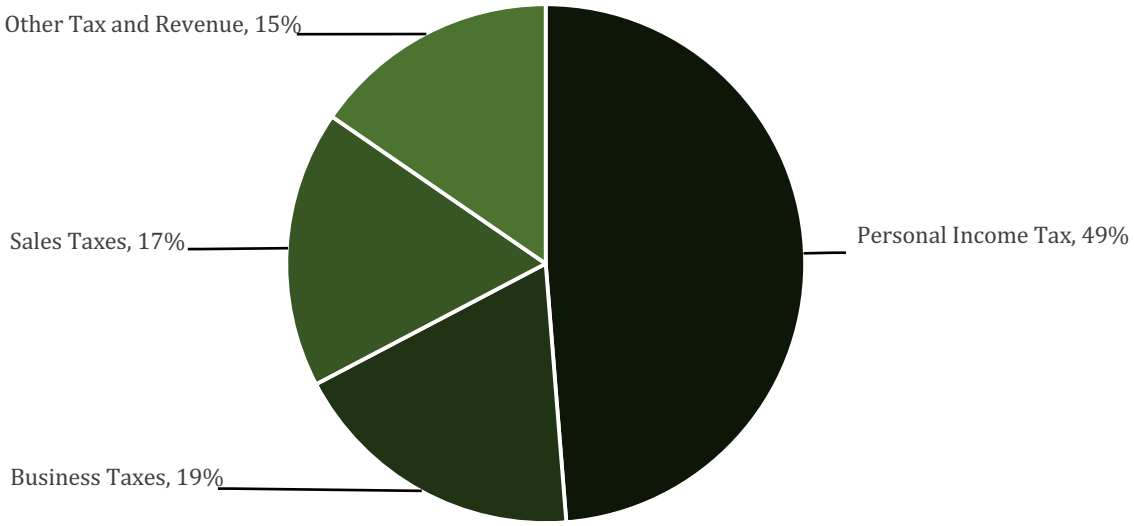
[30] U.S. Census Bureau, "Methodology Updates for the Vintage 2022 Estimates" (webinar December 2022).

[31] Cornell Program on Applied Demographics, *Analysis of the US Census Bureau Vintage 2021 Total County Population Estimates* (March 2022), https://pad.human.cornell.edu/papers/downloads/V2021highlights.pdf.

The Executive Budget Financial Plan

State Operating Funds: Receipts

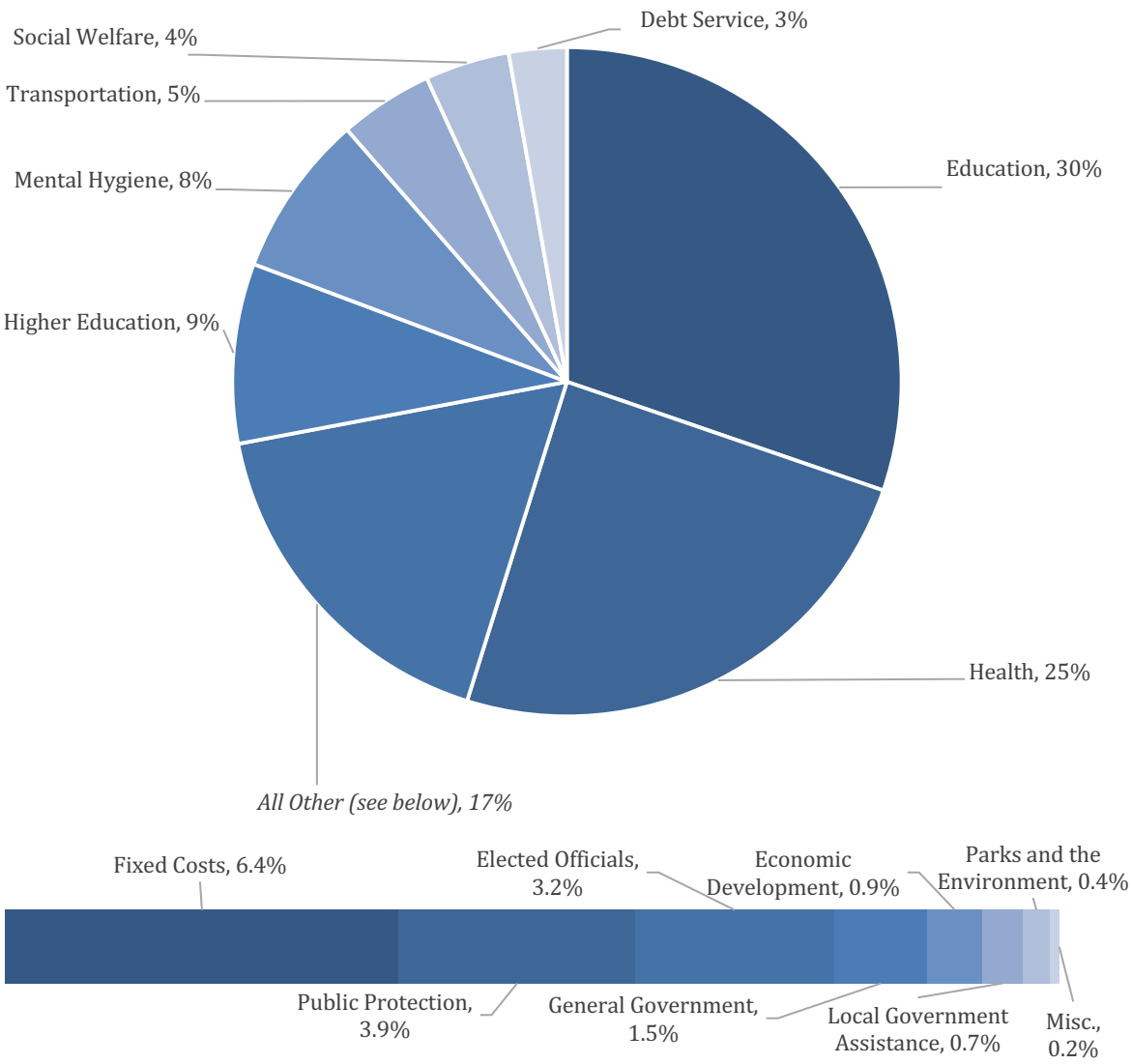
Receipts by Source, Fiscal Year 2024
$125.8 Billion



State Operating Funds: Expenditures

Spending by Program Area, Fiscal Year 2024

$125.2 Billion



Financial Plan in Detail

The Executive Budget heads into fiscal year 2024 with a projected surplus from fiscal year 2023 of $8.7 billion, while anticipating sizable outyear gaps.[1] These projected gaps result primarily from downward revisions to future tax receipts.

Figure 1. Fiscal balance, fiscal years 2023 to 2027

Fiscal Year Surpluses/(Gaps) *Dollars in billions*					
Fiscal Year	**2023**	**2024**	**2025**	**2026**	**2027**
End of Year Balance	$8.7	0	($5.7)	($9.0)	($7.5)

The executive budget uses the fiscal year 2023 surplus of $8.7 billion to accelerate $5.4 billion of planned deposits into the state's reserve funds. By prepaying reserve deposits of $2.4 billion and $2.9 billion planned for fiscal years 2024 and 2025, respectively, the budget frees those resources across both years. The budget also deposits $1.0 billion into the debt reduction reserve fund and shifts a planned $900 million debt service prepayment from fiscal year 2024 to 2023. These prepayments bring the fiscal year 2023 and 2024 budgets into balance: surpluses are reflected by higher expenditures (as in the case of debt service payments) or transfers to other funds (as in the case of reserve deposits). In making these prepayments, however, the surplus opens fiscal space in fiscal years 2024 and 2025, lowering planned debt service spending and reserve fund deposits.

These fiscal year 2023 savings, together with modest revenue action, support fiscal year 2024 despite weakening expected revenue. The executive budget expects state operating funds revenue in fiscal year 2024 to fall $2.6 billion — 2.0 percent — from 2023 levels. While the executive budget expects fiscal year 2024 PIT and sales tax receipts to rise slightly from 2023, this is more than offset by falling revenue from business taxes and miscellaneous receipts. Lower business tax receipts are the result of a projected decline in partnership income and corporate profits driving down pass-through entity tax (PTET) and corporate franchise tax (CFT) revenue, respectively.

Revenue in the outyears — fiscal years 2025 through 2027 — was revised significantly downward significantly between projections for fiscal years 2023 and 2024. Both personal income tax and business tax receipts are revised downwards in these projections, resulting in an average of $6.2 billion lower total state operating funds revenue for each of the three outyears. The increase in outyear budget gaps between fiscal year 2023 and 2024 projections is entirely the result of lower PIT and business tax revenue projections, not revisions to spending.

The executive budget's lower revenue estimates are the result of DOB's downward revisions to the state's economic outlook over the next several years. Fiscal year 2025 real personal income growth and employment growth projections, for instance, were revised down by 0.1 percentage points and 0.4 percentage points, respectively between the fiscal year 2023 enacted budget and fiscal year 2024 executive budget. In particular, bonus income and business profits are revised downwards. These downward economic revisions resulted in a $6.9 billion — 5.1 percent — reduction in expected state revenue.

Figure 2. FY 2023 enacted budget vs. FY 2024 executive budget economic and fiscal projections

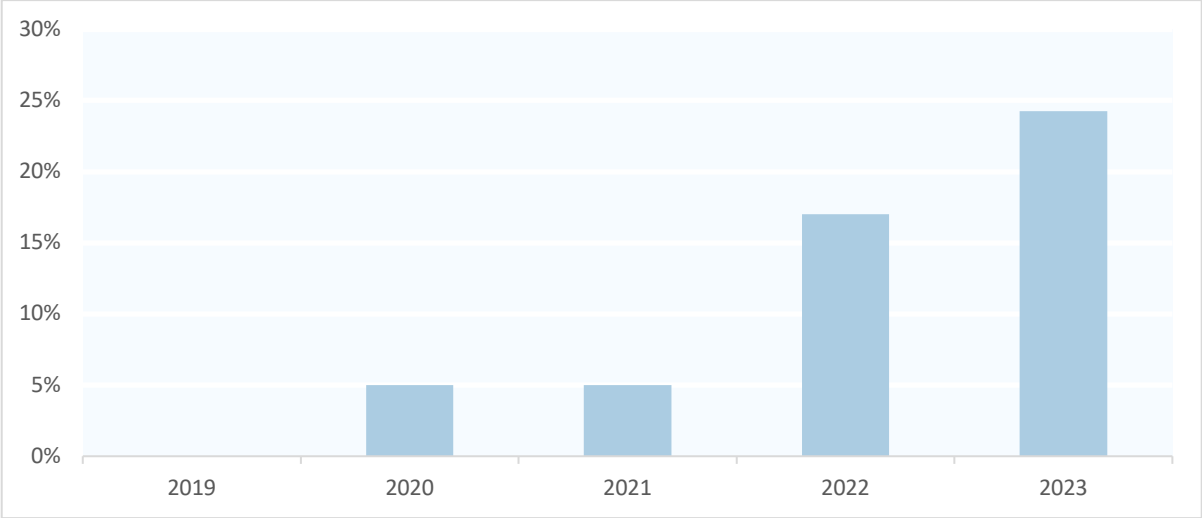
		FY 2024	FY 2025	FY 2026
FY 2023 Enacted	Personal income growth	4.5%	4.5%	4.5%
	Total employment growth	1.4%	1.1%	0.9%
	State revenue	$129.6	$134.7	$133.4
FY 2024 Executive	Personal income growth	4.5%	4.4%	4.2%
	Total employment growth	0.2%	0.7%	0.7%
	State revenue	$125.8	$127.8	$127.7

Personal Income Tax Receipts in FY 2023 Exceed Projections

The executive budget expects fiscal year 2023 revenue to significantly exceed projections made in the fiscal year 2023 enacted budget. Fiscal year 2023 is expected to close with state operating revenue of $128.4 billion — $12.4 billion, or 10.7 percent — higher than the level projected at the beginning of the fiscal year. Higher fiscal year 2023 revenue is almost entirely attributable to strong personal income tax (PIT) receipts. The fiscal year's $58.4 billion in PIT revenue exceeded initial projections by $11.4 billion (24.3 percent).

The fiscal year's higher-than-expected PIT reflects a continuation of Covid-era PIT surpluses. Prior to Covid, actual PIT revenue was generally close to enacted budget projections. In recent years, however, conservative enacted budget projections have consistently underestimated PIT revenue. Fiscal year 2023's 24.3 percent PIT surplus follows the prior year's 17.0 percent surplus.

Figure 3: Actual PIT revenue in excess of enacted financial plan projections, fiscal years 2019 to 2023



The Executive Budget Extends the Corporate Tax and Raises the Payroll Mobility Tax

Downward revisions to corporate tax revenue are especially noteworthy because the executive budget proposes a three-year extension of higher CFT rates enacted in fiscal year 2022. Revenue brought in by this extension would be included in the fiscal year 2024 executive budget revenue projections, but not in any prior projections. The state Division of Budget (DOB) expects these higher rates to bring in $810 million fiscal year 2025, $1.2 billion in fiscal year 2026, and $880 million in fiscal year 2027. The three-year extension would push the rates from expiring in tax year 2024, which would begin affecting fiscal year 2024 revenue and take full effect fiscal year 2025, to a tax year 2027 expiration. This means the expiration will have a marginal effect on revenue in fiscal year 2027, the last outyear for which the executive budget makes projections.

The executive budget proposes another significant revenue action: raising the metropolitan commuter transportation district (MCTD) payroll tax to provide additional operating support to the Metropolitan Transportation Authority (MTA). The MCTD tax funds the MTA budget directly, and is not included in the state operating budget. The proposed change will be discussed in detail in this briefing's transportation section.

Figure 4. State Operating Funds Revenue, Fiscal Year 2023 and 2024 Projections

Dollars in billions

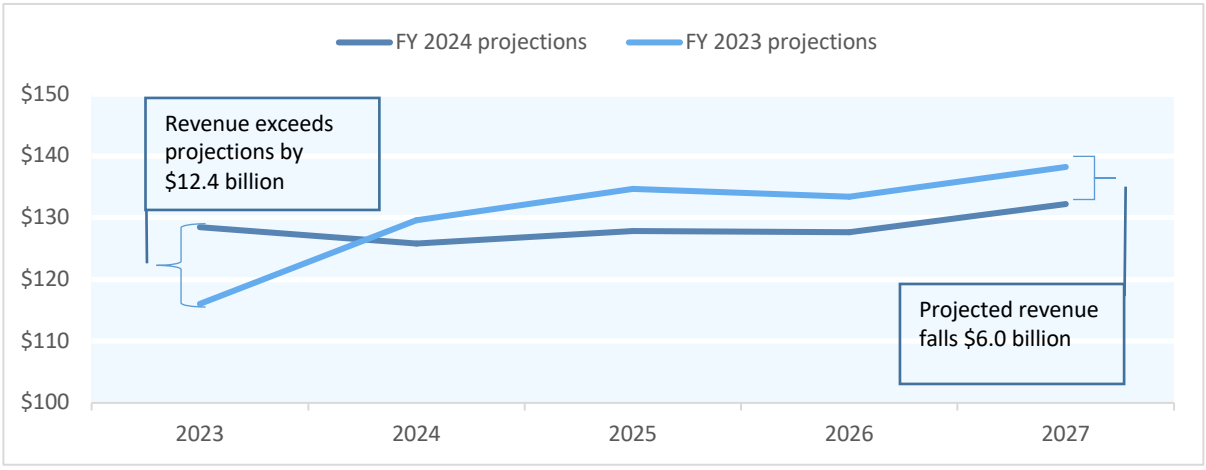


Figure 5. Personal Income Tax Revenue, Fiscal Year 2023 and 2024 Projections

Dollars in billions

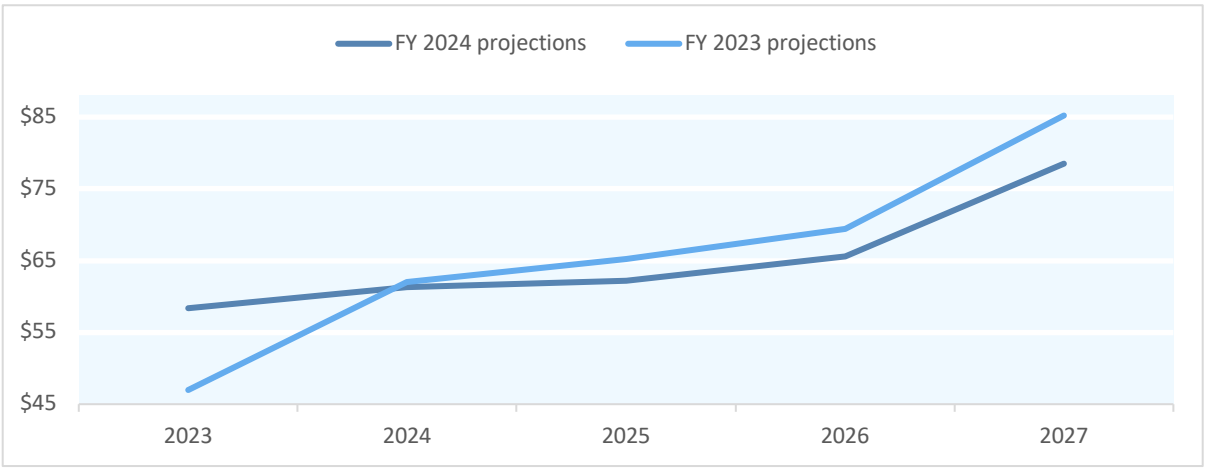
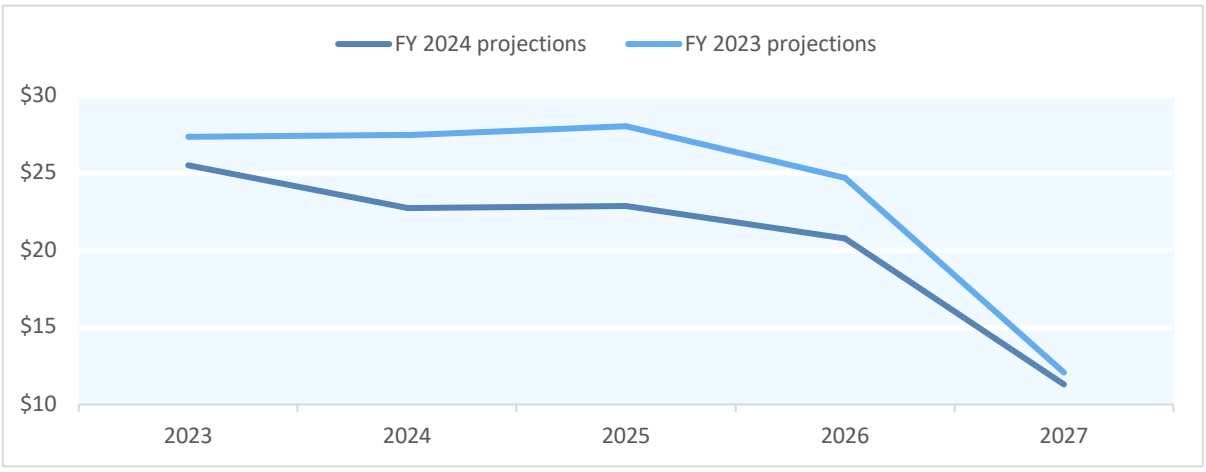


Figure 6. Business Tax Revenue, Fiscal Year 2023 and 2024 Projections

Dollars in billions



Breakdown of State Operating Funds

The budget would raise state operating funds spending by 2.0 percent; this spending would represent a decrease of 1.4 percent, after adjusting for inflation.

The Executive Budget proposes total state operating funds of $125.2 billion in fiscal year 2024, an increase of $2.5 billion, or 2.0 percent, over fiscal year 2023. Given high recent inflation, this spending would represent a decrease of 1.4 percent, after adjusting for inflation. Spending growth is concentrated in the state's two major spending programs: Medicaid and school aid.

Fiscal year 2023 debt prepayments lower fiscal year 2024 debt service to $3.5 billion — $5 billion less than the prior year. These savings, together with continued higher corporate tax rates created fiscal space in the budget, allowing the state to slightly raise spending in other programmatic areas, including transportation and services for asylum seekers.

Increases to School Aid & Medicaid

The executive budget proposes spending $34.4 billion on school aid in fiscal year 2024, an increase of $3.1 billion – 10 percent – from the prior year. School aid primarily consists of foundation aid, which is based on a formula that allocates resources such that all students in the state receive a sound basic education. While the state adopted the foundation aid formula in 2007, fiscal year 2024 foundation aid funding would be the first time the formula was funded in full.

The state's second largest expenditure, Medicaid, would see its spending rise by $2.9 billion – 9.3 percent – in the executive budget. Medicaid expenditures in fiscal year 2024 and outyears have been revised up as caseloads remain higher than expected. However, the state has also benefited from a continuation of the enhanced Federal Medical Percentage (eFMAP), the federal government's increased share of the state's Medicaid costs that has remained in effect since the beginning of the Covid pandemic. The extension of eFMAP through the end of year will save the state $1.5 billion in Medicaid costs in fiscal year 2024. Notably, the executive budget plans to offset its Medicaid costs by fully using savings from eFMAP rather than passing a portion on to counties, as it has in past years. This change would shift $624 million in Medicaid costs from the state on to county governments.

Other Notable Expenditures

These two programs constitute the majority of new state operating spending. However, the executive budget also proposed additional spending in a range of other policy areas. These spending increases above previously planned state operating funds spending include:

- **Asylum seekers:** $944 million in fiscal year 2024 and $355 million in fiscal year 2025 to reimburse New York City for costs associated with sheltering and supporting asylum seekers.

- **Transportation**: The state is proposing a suite of actions to support the MTA, which is facing significant budget gaps. The state would provide the transit system with $300 million in one-off aid and raise recurring state operating aid by $260 million. The executive budget additionally proposes significant legislation to support the MTA, including requiring increased support from

New York City and increases in a dedicated MTA tax. These legislative proposals will be discussed in detail in this briefing's transportation section.

- **Higher education:** The executive budget would increase funding for SUNY through a number of channels: a one-time payment of $75 million for "transformational initiatives," of which $56 million would be paid in fiscal year 2024; $45 million in recurring operating support, rising to $60 million after fiscal year 2024; and a matching grant program for SUNY endowment funds of up to $500 million, of which $375 million is available in fiscal year 2024. Finally, the state would lift recurring annual operating support for CUNY by $40 million.

- **Mental hygiene**: State operating spending is set to rise $520 million – 9.7 percent. Additional funding is largely allocated to adult mental health services, including the creation of 3,500 beds operated by the Office of Mental Health.

State operating spending reductions proposed in the executive budget are primarily constituted of falling debt service costs. However, the budget proposes cutting spending in other areas, most notably social welfare, which would see funding fall $866.0 million – 14.5 percent – from fiscal year 2023. This decline is almost entirely the result of the expiration of the emergency rental assistance program, a Covid-era program to support low-income renters. State spending on rental assistance totaled $1.1 billion in fiscal year 2023 and is due to fall to $135 million in 2024.

[1] New York State Division of the Budget, *Fiscal Year 2024 Executive Budget Financial Plan* (February 2022), https://www.budget.ny.gov/pubs/archive/fy24/ex/fp/fy24fp-ex.pdf and prior editions.

Executive Budget Policy Proposals

The two largest spending increases in the Executive Budget are the proposed increases in Foundation Aid and the growth in Medicaid spending. These are both ordinary increases, the former resulting from fully phasing-in in the Foundation Aid formula, the latter related to national healthcare cost inflation. Additionally, the Executive Budget includes key signature policy proposals, including (i) the proposal to index the minimum wage to inflation; (ii) numerous expansions of Economic Development Subsidies; (iii) increased eligibility for childcare subsidies; and (iv) a plan to increase housing by 800,000 units.

Indexing the Minimum Wage

The proposal does not account for the last year of high inflation, would limit annual raises to 3% and restrict raises in certain years

The governor's executive budget proposes indexing the state's minimum wage to inflation. Under the proposal, the minimum wage would increase annually with inflation, subject to a series of potential limitations. Indexing the minimum wage to inflation would be a major advancement for the state's workforce. However, beginning the index after a period of historically high inflation would leave the minimum wage's buying power permanently lower than it was when the $15 minimum wage was first adopted. For example, inflation has totaled 12.0 percent over fiscal years 2022 and 2023. Further, the limitations on annual increases would continue to erode the minimum wage's buying power relative to the cost of living over time.

The proposed measure would be the first legislation affecting the minimum wage for all workers since the $15 minimum wage was enacted in fiscal year 2017. The legislation phased-in the $15 wage on different schedules according to employers' size and location within the state. The full $15 wage first took effect for large employers in New York City on December 31, 2018.

For most workers, the minimum wage has remained $15. The proposed index would raise the wage each year by the level of inflation over the preceding twelve months.[1] The proposal includes several limitations on annual increases. Annual increases are capped at three percent in years in which inflation exceeds that level. Further, the proposal includes three breaks that cancel a year's increase altogether: the minimum wage remains unchanged any year in which inflation is negative; unemployment rises by half a percentage point; or employment falls.[2] Finally, the proposal eliminates the current minimum wage law's differential for the home care workers. The existing law raises home care workers' minimum wage to $18 beginning October 1, 2023. The governor's budget proposes holding these workers' wages constant at their current wage of $18 until the general minimum wage reaches that level, at which point the home care wage would match the broader minimum wage.

The first annual increase would occur on December 31, 2023, based on inflation in the twelve month period ending July 31, 2023. The increase is likely to hit the proposal's three percent cap; the Federal Reserve

expects 3.1 percent inflation in 2023. Even without the cap, the law's timing in the wake of high inflation would leave the minimum wage permanently lower than its pre-Covid level, after adjusting for inflation. Further, each year in which the three percent cap or economic breaks takes effect, the minimum wage would permanently fall relative to the cost of living. The law provides no mechanism for the minimum wage to fully catch up to inflation.

Figure 1. Inflation and executive budget minimum wage index, 2019 to 2026

Under the proposed index, the real value of the minimum wage falls by $2.50

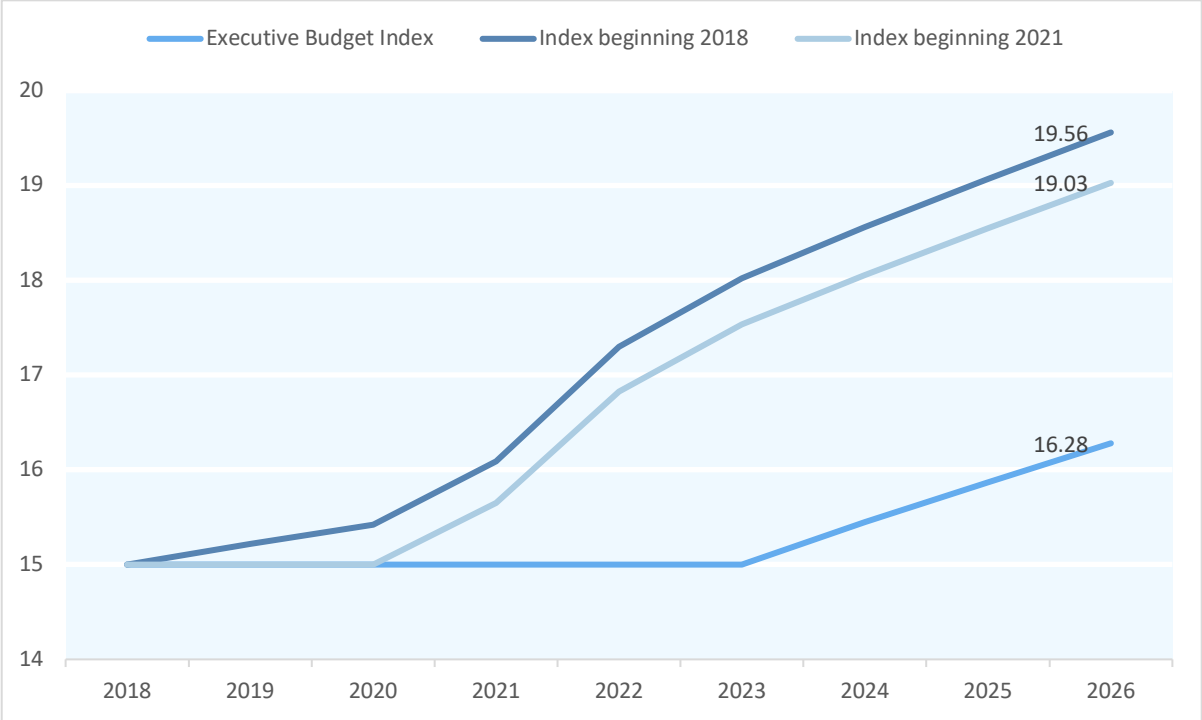
	2019	2020	2021	2022	2023	2024	2025	2026
Inflation	1.4%	1.3%	4.3%	7.5%	*4.2%*	*3.0%*	*2.7%*	*2.6%*
Minimum wage (current dollars)	$15.00	$15.00	$15.00	$15.00	$15.00	$15.45	$15.90	$16.30
Minimum wage (2018 dollars)	$14.79	$14.59	$13.99	$13.01	$12.48	$12.48	$12.48	$12.48

Note: historical inflation from BLS; projected inflation from DOB.[3] FPI projections follow DOB baseline assumption of 2023 recession.

While inflation forecasts suggest that the 2023 minimum wage increase would hit the proposed law's three percent cap, the executive budget economic outlook also makes clear that it expects the economy to enter a recession this year, with unemployment rising by more than 0.5 percentage points. In this case, there would be no annual minimum wage increase in 2023. In this scenario, the state minimum wage would be just $16.30 by 2026, according to DOB inflation estimates.[4] This wage is considerably lower than the $15 wage when it first took effect in 2018. $16.30 dollars in 2026 would be worth just $12.50 adjusted to 2018 dollars—a 16.8 percent decrease in buying power.

By contrast, if the minimum wage had been indexed to inflation starting in 2019, without the proposal's limitations, it would be $19.55 by 2026. If the index began in 2021, to capture recent high inflation, it would be $19.05 by 2026. For a full-time, year-round worker, an additional $2.75 per hour — the differential between the proposed index and one beginning in 2021 without restrictions — would be $5,500 per year, a 16.9 percent increase in annual income.[5]

Figure 2. Current dollar and 2018 dollar level minimum wage under executive proposals and alternative indices



A final element possibly complicates the implementation of the executive budget's proposed minimum wage index. The proposal's wage increase break based on employment appears to rely on data from the Bureau of Labor Statistics' Current Economic Survey (CES). However, monthly CES data is subject to revisions as part of an annual benchmarking process, which adjusts the data to align with more accurate employment indicators. Most recently, the benchmarking revised CES estimates by an average of 0.9 percent across all states.[6] Given that the proposal's employment break cancels an annual increase under any employment decrease, this raises the risk of preliminary data erroneously freezing the wages of New York workers.

Economic Development

New York's economic recovery has advanced considerably since the worst of the Covid crisis. However, unlike the U.S. as a whole, the state has yet to return to pre-pandemic levels of employment, and jobs growth appeared to slow in the second half of 2022. The executive budget has made stimulating economic growth a priority, and proposes a suite of economic development initiatives. These initiatives consist entirely of expanded or revived tax incentives for businesses that make investments or grow employment in New York. Past evidence from these programs has shown that their costs can accumulate over time and persist even after incentives expire or are controlled. Further, the job creation actually attributable to these programs is often underwhelming or unclear.

- **Film tax credit**: Significantly expands the existing film production tax credit. The proposed expansions would raise the credit amount from 25 percent of an eligible film production cost to 30

percent, or 35 percent in the case of relocating television series. The proposal raises the aggregate amount of annual tax credits from $420 million to $700 million from 2024 through 2034, and raises the film post production tax credit from $25 million to $45 million over the same period.

Unlike other tax credits, the film tax credit allows eligible projects to draw future years' credits if the current year's tax credits are fully allocated. By shifting excess costs into subsequent years, this raises costs across the life of the program. Further, the credit's total annual allocation has been increased multiple times in the past, establishing the credit as one of the state's most expensive economic development programs.[7] The state estimates the proposed changes would cost $115 million and $208 million in fiscal years 2026 and 2027, respectively.

- **Extended Prosperity and Innovation Campus (EPIC) program**: Would reboot the 2013 START-UP NY program, which offered tax incentives to new businesses that created jobs on SUNY campuses. START-UP NY eliminated all state and local tax liability for these businesses for ten years. While the program was projected to have no net cost to the state — the jobs created were supposed to be brought into existence only as a result of the benefits — DOB later acknowledged it had spent $53 million advertising the program, and that annual foregone tax revenue exceeded $50 million.[8] The program was credited with creating very few jobs, and in 2017, rebranded and reduced in scope.[9]

  EPIC would reinstate START-UP NY with minor changes. START-UP NY was targeted at Upstate New York campuses and placed limitations on program participation in Downstate New York. EPIC eliminates all regional geographic criteria. The proposal also affords the commissioner of economic development greater authority to approve projects. The program's costs are not capped, and the state has not provided a cost estimate.[10]

- **Small business technology transfer grant program**: Establishes a state tax credit to match tax credits awarded through the federal small business innovation research program or the federal small business technology transfer program. Small businesses awarded either federal grants may be awarded matching state grants. Program criteria therefore follow federal criteria and the proposal does not establish additional rules. The proposal provides broad discretionary power to the Empire State Development Corporation and does not cap total program costs, although the state estimates annual costs to total $6 million.[11]

- **Farmers' Investment Tax Credit**: Allows farmers to receive a refundable Investment Tax Credit (ITC). The ITC provides businesses making capital investments with a tax credit of 4 to 5 percent against investment costs. ITC benefits are already larger for farmers, who receive a 20 percent credit for qualified investment costs. The proposed change would make farmers' ITC refundable, meaning that the value of any credits in excess of recipients' tax liability would be refunded as a cash payment. The executive budget estimates the expansion will cost $7 billion annually.[12]

- **New York City biotech tax credit**: Reinstates a tax credit that had expired in 2019. The state previously authorized New York City to provide biotechnology companies with employees in the city with a tax credit against qualified business expenses. The credit's annual costs capped at $3

million, and reached that cap in recent years. The executive budget authorizes the city to extend this program, without changes, to tax years 2023 through 2025.[13]

- **Micron**: In October 2022, the Governor announced it had reached a deal with Micron, a semiconductor manufacturer, to make a multi-decade, $100 billion investment in Central New York. As part of the deal, New York will provide the company with $6.1 billion in tax incentives — the largest economic development deal in the state's history. Officials expect the deal to eventually yield nine thousand direct jobs.

  The Micron deal follows the enactment of legislation at both the federal and state level to bolster the U.S. semiconductor industry. The Federal CHIPS Act, which created a 25 percent investment tax credit for chip makers and allocated billions more to support their domestic expansion, and New York's Green CHIPS Act were both signed into law in August 2022.[14] The Green CHIPS Act expands the existing Excelsior Jobs Programs, providing chip makers with a suite of tax credits based on business investment and job creation. The program's total costs are capped at $10 billion. The Green CHIPS Act accounts for a large majority — $5.5 billion — of the deal's benefit. The state and Onondaga County, the plant's site, will provide an additional $575 million in infrastructure upgrades.[15] As part of the executive budget, the Governor announced the creation of the Governor's Office of Semiconductor Expansion, Management, and Integration (GO-SEMI) to oversee the deal. This office will be created administratively and has no cost estimate.

- **Belmont Park racetrack**: The state would loan the New York Racing Association, which operates three horse racing tracks in the state, $455 million to renovate its Belmont Park racetrack. As a condition of the financing deal, the New York Racing Association would relinquish its leasehold in the Aqueduct racetrack to the state, allowing the state to redevelop the Queens site.[16] The deal's backers have argued that the loan will carry no cost to the state and generate $1.1 billion in new revenue through greater economic activity.[17] Experts have questioned this analysis's unclear assumptions.[18] The state has not announced its plans for the vacated Aqueduct site.

- **New York City musical and theatrical production tax credit**: Would extend the tax credit, set to expire January 1, 2024, by two years. The existing law allows musical and theatrical productions in New York City to claim a tax credit of 25 percent of production expenses, up to $3 million. The proposed extension would remove an existing provision lowering the maximum benefit to productions beginning after January 1, 2023 to $1.5 million. The proposal would also raise the program's aggregate credits from $200 million to $300 million.[19] The state estimates additional costs would split into $50 million tax expenditures in both fiscal year 2026 and 2027.[20]

Transportation

State and City would each contribute additional $500 million, along with new payroll tax increase and casino revenue — outyear budget gaps continue to pose serious challenges

State Contributions: The executive budget takes a number of spending and legislative actions to close the significant budget gaps facing the MTA. In fiscal year 2024, the state has proposed increasing its operating support to the MTA, raising recurring operating aid by $260 million and providing a one-time $300 million

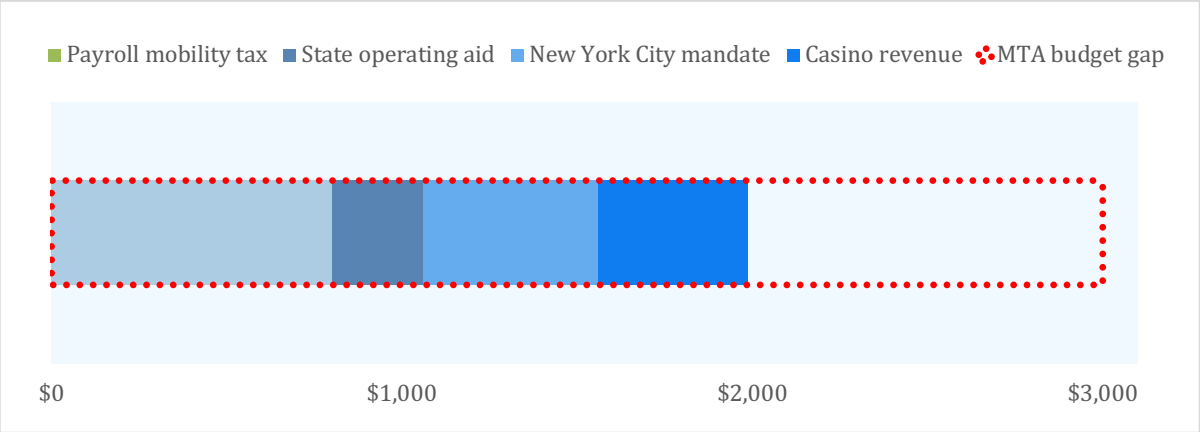
payment. These appropriations would lift fiscal year 2024 state support for the MTA $560 million above the MTA's estimated state operating support for the year of $2.8 billion.[21]

City Contributions: The state would further attempt to fill the MTA's budget gap by mandating recurring $500 million contributions from New York City. The state achieves this mandate by requiring the city to fully fund the MTA's paratransit operations and reduced student fare programs and to fund 47 percent of MTA payroll mobility tax exemption for certain workers. The executive budget financial plan estimates these mandates will total $438 million in the city's fiscal year 2024, although the budget briefing puts this figure at $500 million, and costs associated with the mandate could rise in subsequent years. The proposed legislation authorizes the state to withhold funding from the city if the city fails to fully fund the mandate.[22]

Dedicated Payroll Tax Increase: Proposed legislation would also raise the MTA dedicated payroll tax paid by large employers in the region of the state served by the MTA. Employers with payroll expenses above $437,500 — the tax's top rate — will see their payroll mobility tax rate rise from 0.34 percent to 0.5 percent. Self-employed individuals in the MTA service area with earnings above $50,000 will see their tax on rise from 0.42 percent to 0.5 percent. The executive budget estimates these changes will increase revenue by at least $800 million.

Divert Casino Revenue: Finally, the executive budget would divert expected revenue from the licensing of three new Downstate New York casinos to the MTA. Under the state's existing casino revenue statute, 80 percent of funds would be spent on school aid or property tax relief, with remaining revenue split between the local governments hosting the casino. A proposed change would direct all revenue from new casinos located within New York City and 80 percent of revenue from new Downstate casinos not located in the city to the MTA.[23] The proposal does not include firm revenue estimates, although the executive budget briefing book estimates $1.5 billion in immediate revenue from licensing fees and $462 to $826 million in annual revenue thereafter. The revenue will not materialize until at least 2026.[24]

Figure 3. Additional recurring revenue relative to outyear MTA budget gaps, beginning fiscal year 2025



The MTA's fiscal challenges have grown as federal aid appropriated as Covid relief begins to recede even as ridership remains significantly lower than pre-pandemic levels, depressing fare revenue. The MTA projects a budget gap of $2.8 billion in 2024 rising to $3.0 billion in 2025 and 2026.[25] While the MTA expects remaining federal aid to support operations in 2023 and 2024, larger budget gaps thereafter pose

serious challenges. Additional recurring revenue included in the fiscal year 2024 executive budget totals $2.0 billion to $2.4 billion, depending on recurring casino revenue. While this year's one-off $300 payment and unspecified outyears' casino licensing fee revenue will help close single year gaps, new annually recurring revenue amounts to two-thirds of the MTA's recurring outyear budget gaps. New state aid does not appear to have affected the MTA's proposed 2023 budget, including its planned 5.5 percent fare hikes.[26]

Childcare

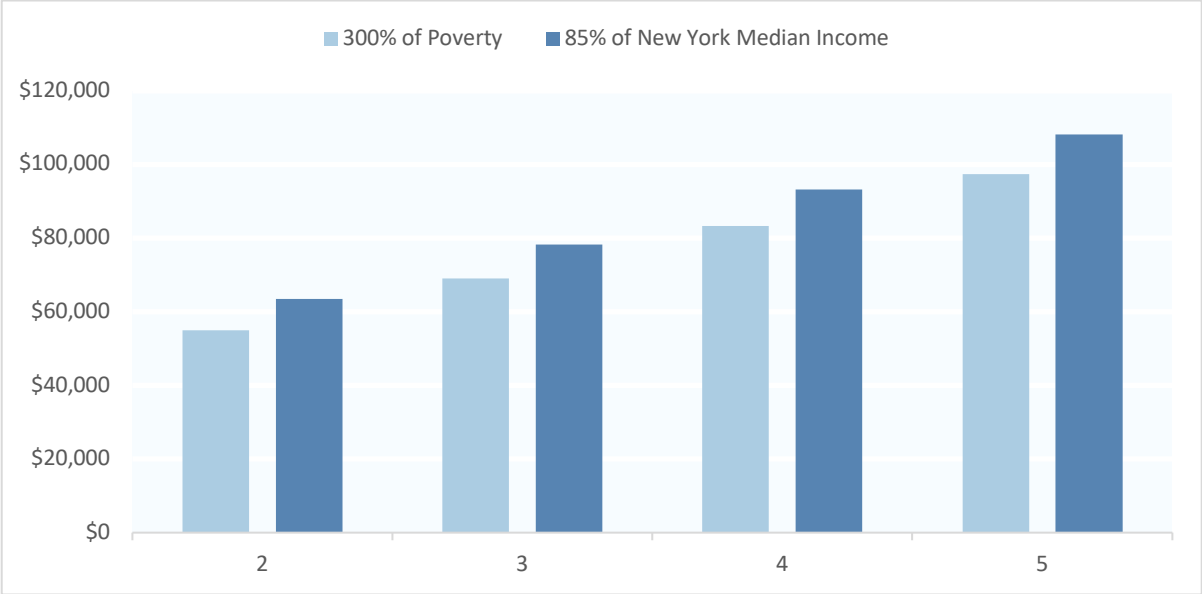
Proposal increases income eligibility limit from $83,000 to $93,000 — 55% of families remain ineligible

Childcare is a growing challenge facing New York. The state's childcare costs are the sixth highest in the U.S. Infant care costs for a middle-income New York family with children total 22.1 percent of income.[27] While costs are high across the state, new data from the U.S. Department of Labor points to a particularly acute crisis in Downstate New York. Seven New York counties, all downstate, are in the top one percent of costliest counties for infant care in the U.S. Two New York counties, the Bronx and Brooklyn, have higher infant care costs as a percentage of income than any other county in the U.S., while Queens is fourth in the nation.[28]

The state has taken steps in recent years to counteract these trends. In fiscal year 2023, the state raised the income threshold for families to be eligible for state subsidized childcare from 200 percent of the federal poverty measure to 300 percent. The state also increased payment rates for subsidized childcare from 69th percentile of the market to 80th percentile.[29] Both changes incrementally expand access to childcare for low- and moderate-income families. The state estimated these changes would cost $290 million annually.[30]

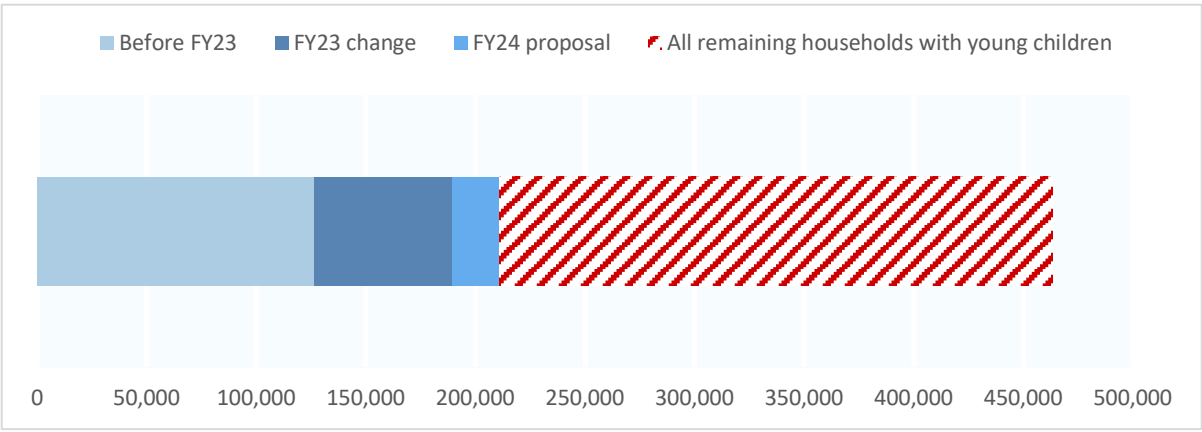
The fiscal year 2024 executive budget would continue incrementally expanding access to childcare. The budget proposes raising the eligibility threshold for state-funded subsidized childcare from 300 percent of the federal poverty measure to 85 percent of the New York State median income. For a family of four, this would increase the limit for eligibility from $83,250 to $93,259.[31] While the executive budget does not provide cost estimates for expanding eligibility, it raises the proposed state operating funds local assistance spending of the Office of Children and Family Services, the agency that administers the state Child Care Block Grant, by $132.9 million – 7.4 percent above fiscal year 2022 spending – to $1.9 billion.[32]

Figure 4. Current and proposed income thresholds for state-subsidized childcare eligibility by family size



FPI estimates that the proposed change would expand eligibility to about 21,700 New York households with children under age 6. These households represent 4.7 percent of all such households. By contrast, fiscal year 2023's eligibility increase expanded the access to the program to 63,000 households — 13.6 percent of all households with young children. If the proposed changes are adopted, 252,500 households with young children — 54.5 percent — would remain above the eligibility threshold.[33]

Figure 5. Number of households with young children eligible for state-subsidized childcare under former, current, and proposed eligibility thresholds



The executive budget also proposes a new tax credit to expand the supply of childcare providers. The proposed Child Care Creation and Expansion Tax Credit Program would create a tax benefit for childcare providers that create new childcare capacity in New York State. Tax credits would cover 20 percent of the state-subsidized childcare reimbursement rate. Total tax credit costs are capped at $25 million annually. The proposal authorizes the law for just two years: childcare providers must create seats by the end of 2024 to benefit from the credits.[34]

Housing

New York has long faced an acute housing crisis. More than one-quarter (27.7 percent) of New York renters pay half their income to rent. This high percentage of severely rent burdened New Yorkers is also the third-highest among U.S. states. Further, half (50.3 percent) of the state's renters pay 30 percent or more of their income to rent, the sixth-highest share in the U.S.[35] As this briefing book documented in its analysis of the state' s population trends, housing costs are a key driver of population loss. Recent years have seen an uptick in population outflow, with significant movement towards out-of-state suburbs of the New York metropolitan area. While this trend has unclear fiscal implications for the state, as many movers likely continue to hold New York jobs, they unambiguously represent revenue losses for local governments.

The executive budget proposes a suite of policies to counter these trends. The proposed changes are primarily legislative, affecting local land use and tax policy with the goal of increasing housing production, especially in Downstate New York. The budget includes a $250 million fund to support localities make infrastructure improvements and other changes necessary to support more housing. The executive budget's major local land use policies include:

- **New Home Targets and Fast-track Approval Act**: beginning in 2024, local governments would be required to meet three-year housing production targets. Downstate counties would be required to grow their housing stock by three percent every three years. Upstate counties must grow by one percent. New income-restricted housing units are counted as two units towards the targets, while rehabilitated abandoned property are counted as 1.5 units.

  The law designates localities that meet their housing production targets or undertake any two of a prescribed list of policy actions that increase housing production as "safe harbors." The five policies prescribed by the proposal consist of changes to local land use law, with specific metrics for the density of newly-permitted housing. Localities that do not qualify as safe harbors at the end of the first three-year cycle would be required to approve qualifying applications to build residential housing, regardless of whether the application complies with local land use laws. The law establishes affordability criteria for projects qualified to override local land use laws in non-complying jurisdictions.[36]

- **Transit-oriented Development Act of 2023**: establishes "aggregate density requirements" for the area adjacent to Downstate transit. The proposal would set housing density requirements for the half-mile radius around transit stations, based on stations' distance from New York City. Localities would be required to approve qualifying projects for transit zones under the prescribed housing density.

  The first of the four tiers carries the highest density requirements of 50 housing units per acre and includes transit stations in the city or within 15 miles of the city border. Density requirements lessen through the fourth tier, which requires 15 housing units per acre near transit stations served by any Downstate transit authority and is more than 50 miles from the city.[37]

In addition to these major changes to local land use, the executive budget proposal includes new and amended tax credits to spur housing production. Each proposal would authorize local tax incentives. As such, they carry no cost to the state. The budget does not provide estimates of costs to local governments.

- **New York City Building Improvement Tax Abatement**: authorizes New York City to administer a new tax abatement. Eligible buildings, including rental buildings that are owned by limited-profit entities or include 50 percent income-restricted units and homeownership buildings, would qualify for a property tax abatement of up to 70 percent of the costs of capital improvement construction, taken over up to 20 years. The annual amount of the abatement would be non-refundable and capped at 8 and one-third of construction costs.[38]

- **Multifamily Building Tax Exemption**: authorizes localities other than New York City to exempt newly built multifamily buildings from local property taxes. Eligible buildings must include at least 20 percent income-restricted units. Once completed, buildings would be eligible for tax exemptions for that phase out over a 25 year period.[39]

- **Accessory Dwelling Unit Tax Exemption**: authorizes localities to create a tax benefit for existing residential buildings that create one or more accessory dwelling units. Such buildings would receive a property tax exemption on the increase in property value attributable to the new units, up to $200,000 in assessed value. The law would provide a 100 percent exemption for five years, followed by a five year phase-out.[40]

- **New York City affordable housing from commercial conversions tax incentive**: authorizes New York City to create a new property tax exemption for the conversion of non-residential buildings to affordable housing. To be eligible, non-residential buildings converting to residential must set aside 20 percent of newly created housing units as income-restricted. The proposal sets affordability levels, including that five percent of new units must be deeply affordable. Qualifying projects would benefit from a 19-year benefit period, with core Manhattan projects receiving a 50 percent exemption and all projects receiving a 35 percent exemption.[41]

Finally, the executive budget proposes further legislation aimed at increasing the supply of housing. These include:

- Requiring local zoning authorities to provide detailed zoning information to the state.[42]
- Expanding the criteria under which local governments may consider housing as abandoned.[43]
- Permitting the conversion of commercial buildings in New York City to residential.[44]
- Allowing New York City to legalize basement dwelling units.[45]
- Allowing New York City to override the existing state-imposed floor area ratio cap for residential buildings.[46]

The executive budget's two proposed laws setting housing production and transit-adjacent density targets would represent unprecedented state action to increase the supply of housing in Downstate New York. These proposals would primarily produce market rate housing. As such, they would be especially consequential for middle- and upper-middle-income New Yorkers who nevertheless face significant housing price constraints in, and often move out of, Downstate New York. Supply alone would not fully

address the needs of moderate- and lower-income New Yorkers. While several of the executive budget's tax benefit proposals contain affordability requirements, they would authorize localities to adopt them. The localities would then have to weigh the programs' cost against other strategies to create affordable housing. Finally, it is notable that the executive budget allows $990 million in state-funded rental assistance programs passed in fiscal year 2022 to expire.

Reserves

Accelerated deposits to the state's long-inadequate fiscal reserves open fiscal space in fiscal years 2024 and 2025

New York has historically lagged on funding its fiscal reserve funds, leaving the state more vulnerable to economic downturns. Since Covid, the state has begun to take fiscal reserve funding seriously. The fiscal year 2024 executive budget takes further steps to build the state's reserves, prepaying planned deposits and proposing changes to the reserve fund's statute. These changes would bring the reserves up to long-term target balances and freeing fiscal space in fiscal years 2024 and 2025. This fulfills the reserves' core purpose: smooth revenue over time and allow recurring revenue to support a higher base of recurring spending. Building reserves with non-recurring or high-than-expected revenue, rather than recurring deposits, affords the state greater fiscal flexibility.

Maintaining sufficient reserves is sound fiscal policy as economic downturns take severe tolls on state budgets. Unlike the federal government, state law generally requires that states run balanced budgets and imposes constitutional limitations on the ability to borrow to cover budget shortfalls. Because of this, in the face of fiscal shortfalls, states must enact spending cuts, tax increases, or a combination of the two. To avoid or mitigate these choices, states typically set aside revenue during economic expansions as fiscal reserves. In turn, these reserves, or rainy day funds, can be used to cover revenue losses during economic downturns, allowing states to maintain public services.

Balancing the goal of sufficient fiscal reserves and fully funding public services, however, can be challenging under uncertain economic conditions. In making decisions about the pace of deposits to reserve funds given expected economic conditions, policymakers should consider the core goal of reserve funds: to maintain services funding during economic downturns. Restraining services funding for the sake of reserves funding runs counter to the core purpose of the reserves. Conversely, taking advantage of non-recurring and unexpectedly-high revenue to build reserves and fully funding recurring services out of recurring revenue would balance these goals.

Fiscal reserves in New York: recent trends and policy changes

In recent decades, New York's fiscal reserves were inadequately maintained. Immediately prior to the 2007-09 recession, New York's reserve funds as a share of annual general fund spending were 40th among U.S. states. On the eve of the Covid crisis, they were the 9th lowest.[47] Inadequate reserves left New York uniquely exposed to both of these crises. Without reserves, the state relied on spending cuts, tax increases, and federal relief to balance recession-era budgets. Federal relief played an important role during both

crises. However, Congress enacted this relief on a discretionary basis, creating uncertainty at the time and little assurance about relief in future crises.

Since Covid, New York policymakers have made a more concerted effort to build reserves. With its budget buoyed by unprecedented federal fiscal relief, New York deposited more than $5 billion into its reserve funds in both fiscal year 2022 and 2023 — the largest expansion of the funds since the enactment of the rainy day reserve funds.

Despite this expansion, New York's reserves remained below most other states, which similarly used federal funding to build reserves. In fiscal year 2023, the median state's reserve levels as a share of spending were 5.0 percentage points above New York's reserves, despite its recent deposits. New York remained the 9th lowest state in the U.S. by this measure.[48]

New York also remained below its own goals for reserve funding levels. In a 2019 report, the New York State Comptroller recommended that the state set aside 10 percent of annual general fund spending.[49] Deposits made in fiscal year 2023 brought this level to 6.9 percent, three percentage points higher than fiscal year 2022.

In fiscal year 2023, lawmakers set a more ambitious target: to build reserves totaling 15 percent of state operating funds spending, a broader spending measure, by fiscal year 2015.[50] To enable this target, lawmakers raised the maximum balance authorized for the rainy day reserve fund, the state's primary fund for fiscal reserves. In addition to the rainy day fund, the state maintains other funds with differing levels of restrictions on the deposits and withdrawals. These funds include:

- **Rainy Day Reserve Fund (RDRF):** the state's primary fiscal reserve fund, RDRF can be tapped after five consecutive months of decline of an economic index composed of private sector employment, the state unemployment rate, manufacturing hours worked, and sales tax collections.[51] Since 1970 — the beginning of the period tracked by the index — New York recessions have closely aligned with U.S. recessions. The five month rule imposed by the law authorizing the RDRF has delayed the statutory availability of the RDRF relative to U.S. recessions in every post-1970 recession but one (the recession beginning in 1989).[52] However, U.S. recessions themselves are not declared contemporaneously, but as high-quality data becomes available. In fiscal year 2023, lawmakers raised that maximum allowable RSRF balance from five percent of general fund spending to 15 percent. The RSRF statute allows for deposits of up to three percent of general fund spending per year.

- **Tax Stabilization Reserve Fund (TSRF):** TSRF rules are more mechanical than the RDRF. TSRF rules require any general fund surplus to be deposited into the fund, up to 0.2 percent per year. The total fund balance is limited to two percent of annual general fund spending. If general fund revenue falls below spending at the end of the fiscal year, funds are transferred from the TSRF to fill the gaps.[53] The New York State Division of Budget (DOB) refers to the TSRF and RDRF collectively as "rainy day reserves."

- **Economic uncertainties:** beyond the two statutory reserve funds, DOB includes funds set aside for "economic uncertainties" as constituting the state's principal reserves. These funds do not exist

under statute, but are unrestricted general fund reserves that can be carried forward across years. Allows for the most flexibility, but the goal in recent years has been to formalize reserves by making deposits to RDRF.

Reserve funds in the fiscal year 2024 executive budget

The executive budget proposes using a majority of fiscal year 2023's surplus revenue to fund the state's fiscal reserves. The fiscal year 2023 enacted budget financial plan budgeted deposits of $2.4 billion and $2.9 billion planned for fiscal years 2024 and 2025, respectively. The governor's fiscal year 2024 proposal would prepay this collective $5.4 billion deposit out of current year surpluses and zero out reserve contributions for fiscal year 2024 and subsequent years.

Notably, statutory limits on the size of annual reserve deposits require that these surplus funds are deposited to the unrestricted economic uncertainties fund rather than the statutory RDRF. The updated fiscal year 2024 reserves plan would keep the RDRF balance permanently lower than the balanced planned in fiscal year 2023 budget.

The executive budget proposes legislation to change these deposit limitations. The proposals would increase the maximum annual deposit to the RDRF from three percent of general fund spending to 10 percent of state operating funds spending, and raise maximum total fund balance from 15 percent of the general fund to 20 percent state operating funds. State operating funds is a larger budgetary category than the general funds (state operating funds are comprised of the general fund, debt service, and the state's special revenue funds).[54] As such, these reforms allow the state to significantly increase annual deposits and the total balance of the RDRF.

Figure 6. fiscal reserve balances planned in fiscal year 2023 enacted budget and fiscal year executive budget

		2018	2019	2020	2021	2022	2023	2024	2025
FY 2024 plan	Rainy day reserves	$1,798	$2,048	$2,476	$2,476	$3,319	$6,468	$9,776	$13,270
	Economic uncertainties	-	-	$890	$1,490	$5,665	$7,570	$6,710	$6,141
	Total principle reserves	$1,798	$2,048	$3,366	$3,966	$8,984	$14,038	$16,486	$19,411
FY 2023 plan	Rainy day reserves	-					$6,468	$6,468	$6,468
	Economic uncertainties	-					$13,070	$13,070	$13,070
	Total principle reserves	-					$19,538	$19,538	$19,538

[1] Inflation measure used is the Consumer Price Index for urban wage earners and clerical workers (CPI-W) for the Northeast U.S. The Bureau of Labor Statistics developed the CPI-W subcomponent to serve as an index for social security payments. It gauges spending of lower and moderate income workers and has generally increased in line with, or faster than, the CPI for all urban consumers (CPI-U).

[2] The inflation test is applies if preceding-year CPI-W is negative by July 31st of any year; the unemployment test follows the Sahm Rule: if the three-month moving average state unemployment rate at July 31st is 0.5 percentage points above prior-year lows; the employment test applies if July 31st New York nonfarm employment is lower than its January or April level.

[3] U.S. Bureau Labor Statistics, "CPI Databases" (accessed January 2023), https://www.bls.gov/cpi/data.htm; New York State Division of the Budget, *Fiscal Year 2024 Executive Budget Economic and Revenue Outlook* (February 2022), https://www.budget.ny.gov/pubs/archive/fy24/ex/ero/fy24ero.pdf.

[4] FY24 economic outlook. DOB produces a composite CPI for New York. While this CPI is likely based on CPI-U rather than the proposal's CPI-W, the two series have averaged the same level (2.1 percent and 2.2 percent, respectively) over the last decade. Single-year discrepancies between the two have occurred above 3 percent, which would be null under the proposals. The proposal rounds the minimum wage to the nearest five cents.

[5] Assuming two thousand hours of work per year.

[6] U.S. Bureau of Labor Statistics, *Revisions in State Establishment-based Employment Estimates Effective January 2022* (March 2022), https://www.bls.gov/web/laus/benchmark.pdf.

[7] New York State Division of the Budget, *Fiscal Year 2024 Executive Budget Revenue Article VII Legislation–Part D* (February 2022), https://www.budget.ny.gov/pubs/archive/fy24/ex/artvii/revenue-bill.pdf.

[8] New York State Division of Budget, *FY 2018 Annual Report on New York State Tax Expenditures*, https://www.budget.ny.gov/pubs/archive/fy18archive/exec/fy18ter/TaxExpenditureFY18.pdf.

[9] David Brunori, "Admit It – The Start-Up New York Tax Incentive Program Failed" *Forbes* (August 2016), https://www.forbes.com/sites/taxanalysts/2016/08/01/admit-it-the-start-up-new-york-tax-incentive-program-failed/?sh=513bf64a55a4; Vivian Yee, "Start-up New York Gets a New Name and a Focus on Start-ups" (January 2017), https://www.nytimes.com/2017/01/19/nyregion/start-up-new-york.html.

[10] New York State Division of the Budget, *Fiscal Year 2024 Executive Budget Transportation, Economic Development, and Environmental Conservation Article VII Legislation–Part CC* (February 2022), https://www.budget.ny.gov/pubs/archive/fy24/ex/artvii/ted-bill.pdf.

[11] New York State Division of the Budget, *Fiscal Year 2024 Executive Budget Transportation, Economic Development, and Environmental Conservation Article VII Legislation–Part DD* (February 2022), https://www.budget.ny.gov/pubs/archive/fy24/ex/artvii/ted-bill.pdf.; New York State Division of the Budget, *Fiscal Year 2024 Executive Budget Briefing Book* (February 2022), https://www.budget.ny.gov/pubs/archive/fy24/ex/book/briefingbook.pdf.

[12] New York State Division of the Budget, *Fiscal Year 2024 Executive Budget Revenue Article VII Legislation–Part C* (February 2022), https://www.budget.ny.gov/pubs/archive/fy24/ex/artvii/ted-bill.pdf.; New York State Division of the Budget, *Fiscal Year 2024 Executive Budget Briefing Book* (February 2022), https://www.budget.ny.gov/pubs/archive/fy24/ex/book/briefingbook.pdf.

[13] New York State Division of the Budget, *Fiscal Year 2024 Executive Budget Revenue Article VII Legislation–Part H* (February 2022), https://www.budget.ny.gov/pubs/archive/fy24/ex/artvii/ted-bill.pdf.;City of New York Department of Finance, *Annual Report on Tax Expenditures: Fiscal Year 2022* (February 2022), https://www.nyc.gov/assets/finance/downloads/pdf/reports/reports-tax-expenditure/ter_2022_final.pdf.

[14] Joseph Parilla, Xavier de Souza Briggs, and Mark Muro, "In Central New York, a test of the CHIPS abd Science Act's promise for economic revitalization" *Brookings* (January 2023), https://www.brookings.edu/research/in-central-new-york-a-test-of-the-chips-and-science-acts-promise-for-economic-revitalization/.

[15] Good Jobs First, "Subsidy Tracker Individual Entry–Micron Technology" (accessed January 2023), https://subsidytracker.goodjobsfirst.org/subsidy-tracker/ny-micron-technology.

[16] New York State Division of the Budget, *Fiscal Year 2024 Executive Budget Revenue Article VII Legislation–Part X* (February 2022), https://www.budget.ny.gov/pubs/archive/fy24/ex/artvii/revenue-bill.pdf.

[17] We Are NY Horse Racing, "New Study: Project to build a new Belmont Park will generate $1 billion in economic impact and 3,700 construction jobs" (December 2022), https://www.nyhorseracing.com/belmont-analysis-rls-12-14-22.

[18] Sam Mellins, "Kathy Hochul Bets Half a Billion on Horse Racing. Will the Industry Pay Her Back?" (February 2023), https://www.nysfocus.com/2023/02/07/hochul-horse-racing-subsidy-belmont/.

[19] New York State Division of the Budget, *Fiscal Year 2024 Executive Budget Revenue Article VII Legislation–Part I* (February 2022), https://www.budget.ny.gov/pubs/archive/fy24/ex/artvii/revenue-bill.pdf.

[20] New York State Division of the Budget, *Fiscal Year 2024 Executive Budget Economic and Revenue Outlook* (February 2022), https://www.budget.ny.gov/pubs/archive/fy24/ex/ero/fy24ero.pdf.

[21] Metropolitan Transportation Authority, *MTA 2023 Final Proposed Budget*: *Volume 1* (November 2022), https://new.mta.info/document/101141.

[22] New York State Division of the Budget, *Fiscal Year 2024 Executive Budget Revenue Article VII Legislation–Part D* (February 2022), https://www.budget.ny.gov/pubs/archive/fy24/ex/artvii/revenue-bill.pdf.

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[37] New York State Division of the Budget, *Fiscal Year 2024 Executive Budget Education Labor, and Family Assistance Article VII Legislation–Part G* (February 2022), https://www.budget.ny.gov/pubs/archive/fy24/ex/artvii/elfa-bill.pdf.

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[40] New York State Division of the Budget, *Fiscal Year 2024 Executive Budget Education Labor, and Family Assistance Article VII Legislation–Part O* (February 2022), https://www.budget.ny.gov/pubs/archive/fy24/ex/artvii/elfa-bill.pdf.

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[47] National Association of State Budget Officers, "Historical Data Sets" (accessed January 2023), https://www.nasbo.org/reports-data/historical-data.

[48] National Association of State Budget Officers, "Historical Data Sets" (accessed January 2023), https://www.nasbo.org/reports-data/historical-data. New York's reserves only include rainy day fund reserves, while the New York Division of Budget additionally considers economic uncertainties to comprise reserve funds.

[49] Office of the New York State Comptroller, *The Case for Building New York State's Rainy Day Reserves* (December 2019), https://www.osc.state.ny.us/files/reports/budget/pdf/rainy-day-reserves-2019.pdf.

[50] State operating funds spending includes debt service and special revenue funds administered by the state. The 15 percent target also uses a broader measure of reserve, including rainy day reserves and economic uncertainties funds; the Comptroller measures reserves only as the two statutory rainy day funds. Using the Comptroller's measures, planned rainy day reserves in fiscal year 2025 would total 12.1 percent of planned general fund spending.

[51] State Finance Law, Chapter 56 Article 6, Section 92-CC, https://www.nysenate.gov/legislation/laws/STF/92-CC.

[52] New York State Department of Labor, "Index of Coincident Economic Indicators: December 2022" (accessed January 2023), https://dol.ny.gov/index-coincident-economic-indicators-icei; National Bureau of Economic Research, "US Business Cycle Expansions and Contractions" (accessed January 2023), https://www.nber.org/research/data/us-business-cycle-expansions-and-contractions.

[53] State Finance Law, Chapter 56 Article 6, Section 92, https://www.nysenate.gov/legislation/laws/STF/92.

[54] New York State Division of the Budget, *Fiscal Year 2024 Executive Budget Public Protection and General Government Article VII Legislation–Part CC* (February 2022), https://www.budget.ny.gov/pubs/archive/fy24/ex/artvii/revenue-bill.pdf.

Tax Policy

The Executive Budget proposes no major revenue actions other than extending the current corporate tax rate, which was scheduled to expire at the end of 2023 (and would have led to significant revenue losses). If New York State is going to increase social investment, however, it will be necessary to increase tax revenues on a sustainable, recurring basis.

State tax policy should follow the same fundamental principles of good tax policy that are recognized throughout the world: Taxes should be broad-based and progressive.[1] A tax base is the category that is subject to tax, such as personal income or sales. A broad tax base minimizes exemptions and preferences, thereby maximizing revenue while generally enabling lower tax rates. A broad tax base also prevents economic distortions and promotes fiscal stability. A progressive tax structure imposes increasing tax rates as income or wealth rise, thereby ensuring that the tax burden is shared fairly among different economic groups.

FPI recommends the following policy changes, which are described in greater detail below:

Revenue Recommendations:

1. Increase the progressivity of the personal income tax
2. Impose a surtax on long-term capital gains and dividends
3. Tax capital gains on a mark-to-market basis for high net worth taxpayers
4. Raise the corporate tax rate
5. Tax part of "GILTI" — global intangible low-taxed income — to target multinational profit shifting
6. Reduce the rebate of the pass-through entity tax
7. Reform the estate tax by ending step-up in basis
8. Enable a direct wealth tax

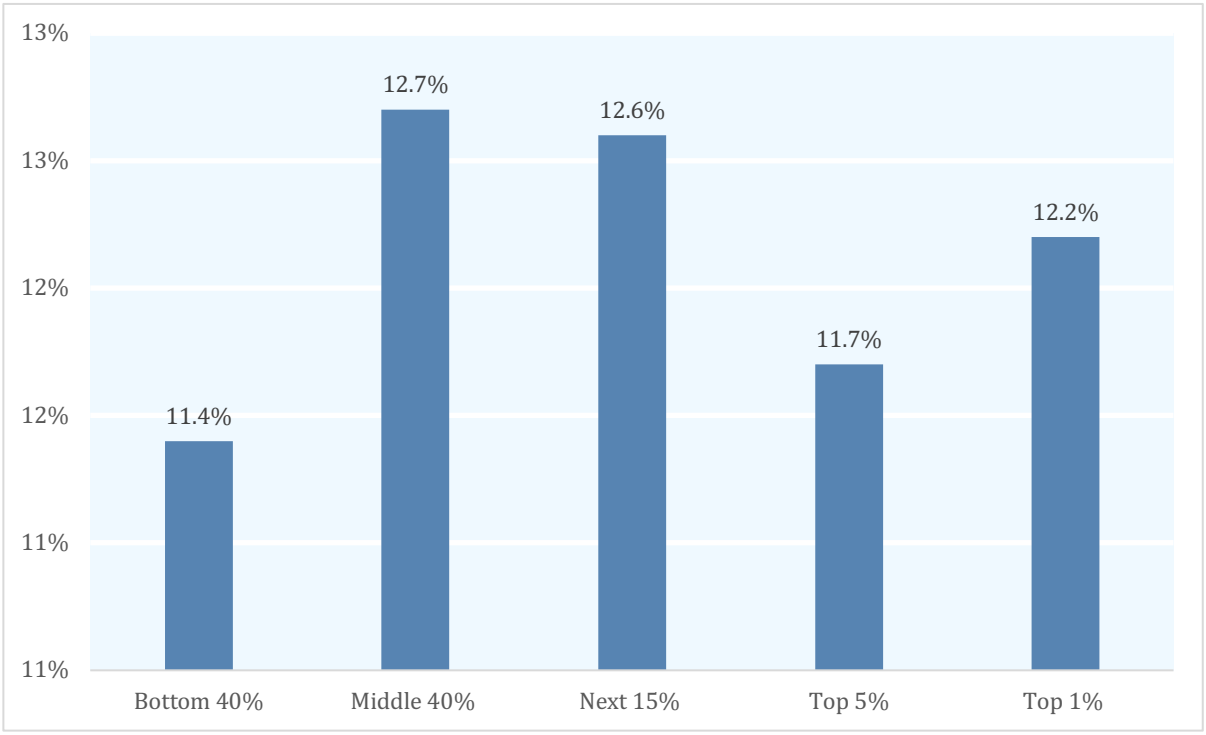
Tax Credit Recommendations:

1. Expand the Empire State Child Credit
2. Fully decouple from the federal tax benefit for Qualified Opportunity Zones
3. Limit the power of Independent Development Agencies to grant tax breaks
4. Reform business tax credits

New York's Regressive Tax Structure

New York's tax system as a whole is regressive, despite its moderately progressive personal income tax. Sales taxes, which are levied at the state and local level, and property taxes, assessed only at the local level, are regressive, taking a larger share of income from the lowest income households. Even after the 2021 personal income tax increases, the wealthy pay a lower combined state and local tax rate than those in middle income brackets, and about the same combined state and local tax rate as the poor. The bottom 40 percent of households and the top 5 percent of households paid nearly the same state and local tax rates of about 11.5 percent, while the middle 55 percent paid a rate of 12.5 to 13 percent.[2] Those who earn more than $1 million per year, less than 1 percent of all tax filers, pay slightly more than 12.2 percent of their income in total taxes. A properly progressive tax system would impose a *greater* burden on higher incomes, based on the principle of the declining marginal utility of income. That is, the first $10,000 of income that a family earns is most valuable because it allows them to pay for the bare essentials such as food and rent; by contrast, the last $10,000 that a millionaire family earns (their earnings over $990,000) has comparatively little value because it can only really be used for investment or luxury consumption.

Figure 1. New York State Tax Burden by Share of Income



Revenue and Expenditure Proposals

Revenue Proposal 1: Increase the Progressivity of the Personal Income Tax

The Personal Income Tax (PIT) is New York's most important source of revenue. In fiscal year 2022, PIT receipts accounted for 58.4 percent of all tax revenue. In turn, PIT revenue is highly dependent on the highest income New York tax filers. This is a result of New York's extreme income inequality as well as its modestly progressive PIT rates. In tax year 2020 (prior to the 2021 higher rates on the "millionaire" brackets), the most recent data available, 128,700 tax filers reported income above $1 million, just 1.2 percent of all tax filers. These filers collectively paid 41.9 percent of all PIT liability.[3]

Prior to the 2008 financial crisis, New York's PIT was flat for all income earned above $40,000.[4] To fill budget gaps created by the ensuing recession, lawmakers created two higher tax brackets on income above $300,000 and $500,000. As the state's fiscal condition improved, PIT rates were lowered for upper-middle class tax filers earning less than $1 million. The fiscal crisis that followed the Covid pandemic created a new impetus for progressive taxation. Lawmakers raised taxes on incomes over $1 million per year and created two new brackets for those earning $5 million and $25 million per year.

Because income and wealth are closely correlated, a progressive PIT is an effective and easily implemented tool to raise revenue from holders of extreme wealth. The recently enacted top PIT rate increases represent the first time the state's rates began to account for the lopsided concentration of resources held at the top of the income and wealth distributions.

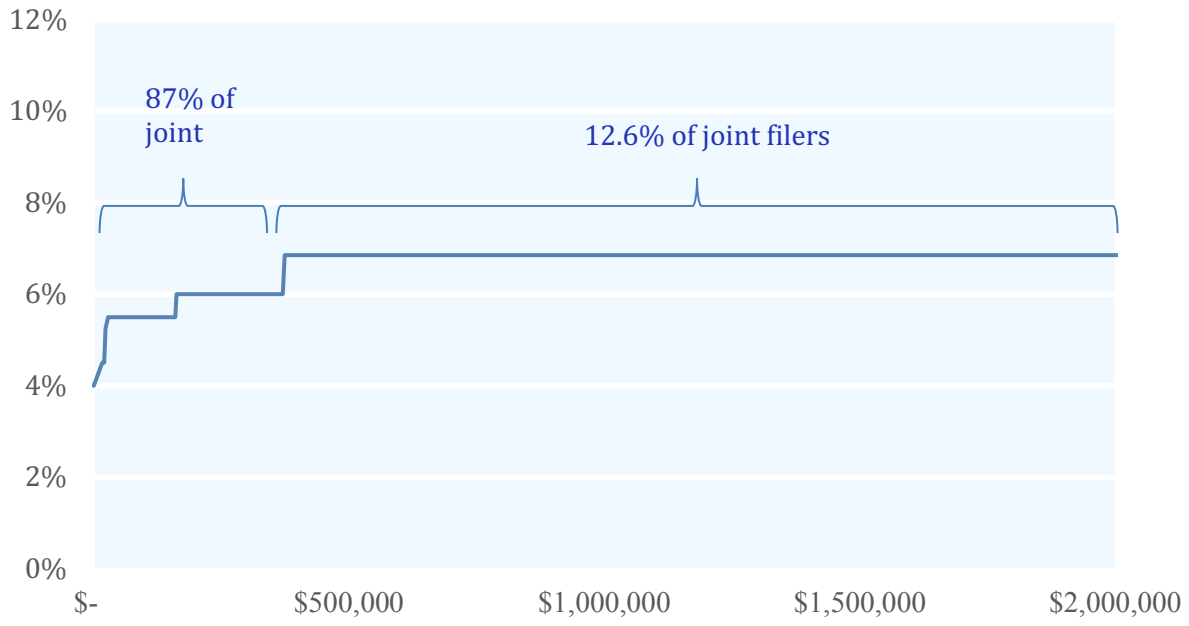
The state can increase the overall progressivity of our tax system, and raise substantial new revenue, by increasing the rates for the "millionaire" brackets (for about $1 million, $5 million, and $25 million in annual income), and restoring the $500,000 tax bracket from the post-financial crisis years. At a minimum, data on extreme wealth suggest that the state should not allow the current PIT rates on the "millionaire" brackets to expire, as they are currently set to, in 2027. While the current structure of the personal income tax is modestly progressive, the number of brackets belies its flatness for most taxpayers. The rates for single and joint filers are as below.

Figure 2. The Current PIT Rate Structure

Single Filer		Joint Filer	
Income	Tax Rate	Income	Tax Rate
$0	4%	$0	4%
$8,500	4.5%	$17,150	4.5%
$11,700	5.25%	$23,600	5.25%
$13,900	5.5%	$27,900	5.5%
$80,650	6.0%	$161,550	6.0%
$215,400	6.85%	$323,200	6.85%
$1,077,550	9.65%	$2,155,350	9.65%
$5,000,000	10.3%	$5,000,000	10.3%
$25,000,000	10.9%	$25,000,000	10.9%

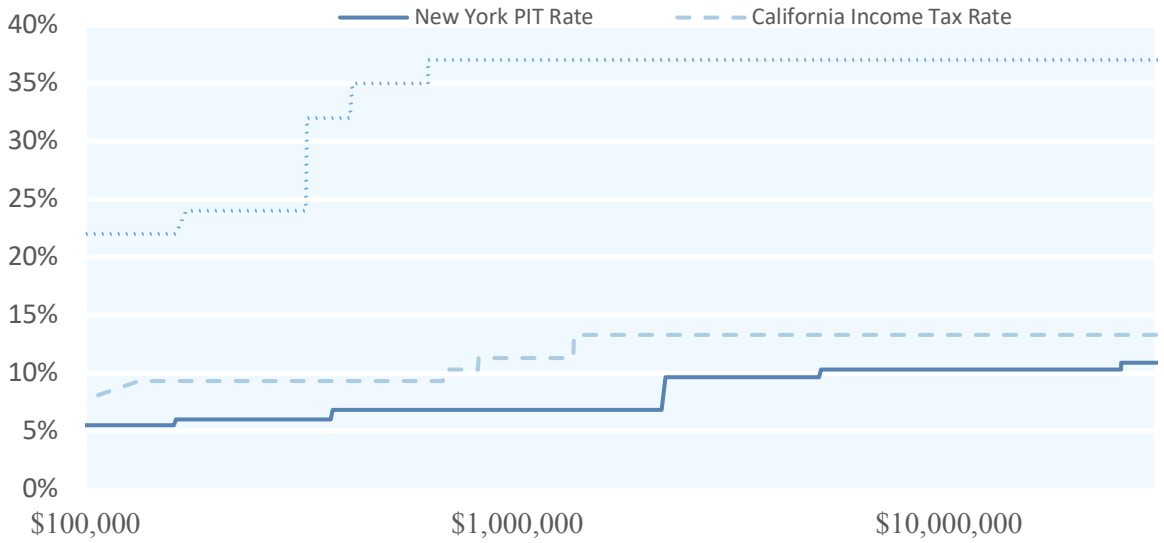
The flatness of the current rate schedule becomes more apparent when depicted graphically.

Figure 3. Personal Income Tax Rates for Joint Filers earning less than $2 million



For joint filers with between $323,200 and $2,155,200 of income, the PIT rate is a flat 6.85 percent. In 2019, about 12.6 percent of all resident joint filers in New York reported income in this range.

Figure 4. Top New York, California, and Federal Income Tax Rates for Joint Filers



New York's higher PIT rates, enacted in 2021, apply to joint filers with over $2.15 million in income (and single filers with over $1.08 million in income). Note that New York's income tax structure, despite these higher rates, is less progressive than both California's income tax and the U.S. federal income tax. The highest tax rate for joint filers in California applies at $1.34 million of income, and the highest federal income tax rate applies at $622,000 of income (for joint filers). By contrast, New York reserves its highest rates for those making over $25 million per year. Adding new brackets and imposing higher rates at lower income levels would both boost revenues and increase overall progressivity.

Revenue Estimates for New PIT Rate Structures

We estimate the three following options for progressive tax increases:

Option 1: Increase Top Rates by 1 Percent

Single Filer		Joint Filer	
Income	Tax Rate	Income	Tax Rate
$0	4%	$0	4%
$8,500	4.5%	$17,150	4.5%
$11,700	5.25%	$23,600	5.25%
$13,900	5.5%	$27,900	5.5%
$80,650	6.0%	$161,550	6.0%
$215,400	6.85%	$323,200	6.85%
$1,077,550	10.65%	$2,155,350	10.65%
$5,000,000	11.30%	$5,000,000	11.30%
$25,000,000	11.90%	$25,000,000	11.90%
Additional Revenue: $1.66 billion[5]			

Option 2: Increase Overall Progressivity and Add New Brackets

Single Filer		Joint Filer	
Income	Tax Rate	Income	Tax Rate
$0	4%	$0	4%
$8,500	4.5%	$17,150	4.5%
$11,700	5.25%	$23,600	5.25%
$13,900	5.5%	$27,900	5.5%
$80,650	6.0%	$161,550	6.0%
$215,400	6.85%	$323,200	6.85%
$500,000	8.0%	$750,000	8.0%
$1,077,550	11.0%	$1,500,000	11.0%
$2,000,000	12.0%	$3,000,000	12.0%
$5,000,000	13.0%	$5,000,000	13.0%
$25,000,000	14.0%	$25,000,000	14.0%
Additional Revenue: $6.66 billion[6]			

Option 3: Very Progressive Income Tax Structure

Single Filer		Joint Filer	
Income	Tax Rate	Income	Tax Rate
$0	4%	$0	4%
$8,500	4.5%	$17,150	4.5%
$11,700	5.25%	$23,600	5.25%
$13,900	5.5%	$27,900	5.5%
$80,650	6.0%	$161,550	6.0%
$215,400	6.85%	$323,200	6.85%
$450,000	7.5%	$500,000	7.50%
$600,000	8.0%	$700,000	8.0%
$700,000	8.5%	$900,000	9.0%
$800,000	9.0%	$1,000,000	10.0%
$900,000	10.0%	$2,000,000	12.0%
$1,000,000	11.0%	$3,000,000	14.0%
$2,000,000	12.0%	$4,000,000	16.0%
$3,000,000	14.0%	$5,000,000	18.0%
$4,000,000	16.0%	$10,000,000	20.0%
$5,000,000	18.0%	$15,000,000	22.0%
$10,000,000	20.0%	$20,000,000	24.0%
$15,000,000	22.0%		
$20,000,000	24.0%		
Additional Revenue: $50 billion[7]			

Options 1 and 2, above, would build on the current structure of the PIT by raising rates on the highest earners. Option 2 would also include a new bracket for those earning under $1 million annually ($500,000 for single filers and $750,000 for joint filers). We estimate that this bracket, on its own, would raise $656 million per year.

Option 3 is considerably more progressive, and would create five new brackets in the sub-$1 million income group, and five new brackets among those earning over $1 million.

Revenue Proposal 2: Raise the Tax Rate on Long-Term Capital Gains

The U.S. federal tax code distinguishes between two types of income: ordinary income, which generally consists of wage and salary income, and capital gain, which is generally income from investments (e.g., the sale of appreciated stock). Where a taxpayer has capital gain that results from the sale of an asset that has been held for longer than one year, the gain is "long-term capital gain" and subject to lower, preferential tax rates. While the top U.S. federal income tax rate is 37 percent for a married couple filing jointly with

earnings over $648,000, the top long-term capital gains rate is 20 percent for a married couple earning over $517,000.[8]

Since 2020, a group of New York legislators have proposed increasing the state tax rate on long-term capital gains and dividends (which receive the same federal tax benefit as long-term capital gains). While New York's Personal Income Tax imposes the same tax rates on ordinary income and capital gain, these legislative proposals have explicitly identified the large federal tax benefit for investment income as the motivation for a long-term capital gains surtax. A state surtax on long-term capital gains could raise substantial revenue, and would offset some or all of the federal tax rate benefit.

We consider three options for increasing the New York State tax rate on long-term capital gains. The options assessed here include: (1) a low surtax rate of 1 percent and 2 percent, (2) moderate surtaxes of 2 percent and 4 percent, and (3) surtaxes of 7.5 percent and 15 percent, as proposed in bill S2162/A2576.

Proposal	Income			Total Revenue[9]
	< $500,000	$500,000-$1,000,000	> $1,000,000	
Low Surtax	0%	1%	2%	$1.66 billion
Moderate Surtax	0%	2%	4%	$3.33 billion
Highest Surtax	0%	7.5%	15%	$12.47 billion

Only 1.3 percent of tax filers in New York would be affected by these proposals, and only 0.83 percent of tax filers would be subject to the highest surtax rate under these proposals (the $1M bracket). This incidence breakdown applies to all three proposals since they have the same income brackets guiding the rate increases. Under any of these three proposals, about 99 percent of tax filers in New York would see zero change in their tax rates.

Revenue Proposal 3: Tax Capital Gains on a Mark-to-Market Basis

In our current tax system, asset appreciation only gives rise to tax liability when the asset is sold. For instance, an individual's stock portfolio might appreciate in value, but no tax is owed until that appreciated stock is sold. While many people think of a sale as the event that gives rise to "income," in economic terms, the income arises as the asset appreciates (because the individual is gaining wealth — the fact that it takes the form of asset appreciation rather than cash is immaterial). However, our tax system treats the sale of the asset as a "realization" event, or the event by which the economic income from asset appreciation gives rise to taxable income. Thus, an ordinary taxpayer with substantial gains in their real estate or stock portfolio does not pay any tax until they actually sell at a profit. This system matches the typical intuition that it would not be fair to tax an individual on unrealized appreciation (especially because taxes must be paid in cash, and thus paying one's taxes could require that they sell the asset solely to pay the tax).

The main flaw in our realization-based system is that it allows individuals to benefit from tremendous asset appreciation without ever incurring tax liability. This is particularly salient with the rise of an ultra-wealthy billionaire class. As ProPublica has reported, most billionaires rarely sell their assets in order to avoid paying tax on their capital gains.[10] Instead, they finance their lifestyle with debt (on which they pay no income tax), deferring their gains until death. Much of this wealth will not be taxed under current law, largely due to the step up in basis rules that eliminate taxable gain when assets are passed on to one's heirs at death. Finally, wealthy individuals often contribute their appreciated assets to private foundations run by their own family members, avoiding tax on their gains while keeping their assets in the family for all practical purposes. ITEP estimates that New Yorkers with more than $30 million in assets collectively hold more $6.7 trillion in wealth, of which more than $3 trillion is unrealized capital gains (46 percent of total wealth).

A "mark-to-market" income tax system would tax asset appreciation as it occurs, rather than waiting for the taxpayer to realize their gains. For instance, if a wealthy individual's investment portfolio grows in value by $10 million over the course of a year, they would be treated as earning $10 million of taxable income in that year.[11]

Implementing a comprehensive mark-to-market income tax on ultra-rich taxpayers would require annual valuations of all assets in order to measure the annual gains. Critics commonly hold that this is practically impossible or else unreasonably burdensome, but tax law scholars have shown how the challenge could be met.[12] Additionally, mark-to-market rules could be applied to all of a taxpayer's historical unrealized gains, or imposed only on a prospective basis. The former option would immediately raise windfall revenue before falling to a baseline annual revenue. A more incremental option would be to only tax current year capital gains on a mark-to-market basis, thereby foregoing the initial windfall revenue. The scope of the tax could be further limited to publicly traded instruments, so as to avoid the challenges of valuing private assets.

On an annual basis, it is estimated that taxing capital gains on a mark-to-market basis would raise about $1.5 billion.

Revenue Proposal 4: Tax the Profits of Pass-Through Businesses

While many people conventionally refer to all businesses as "corporations," the corporation is in fact only one type of business entity. A business can also be organized as a partnership or LLC, known as "pass-through" business structures because of their different tax treatment. A corporation is subject to two levels of taxation on corporate earnings — first, the corporation pays corporate income tax on its net earnings; second, when the corporation distributes its profits to shareholders as dividends, those dividends are taxed as individual income to the shareholders. In a "pass-through" business, by contrast, the income earned by the business is taxed only at the level of the individual business owners; the business itself pays no tax on its entity level income, all of which is treated as earned by the business owners. Most businesses are now formed as partnerships, LLCs, or S-Corporations, all of which are treated as pass-through entities for federal and most state and local income tax purposes.[13]

Historically, and prior to the rise of the limited liability company (the LLC), business owners generally had to choose between forming a corporation and paying the corporate tax or forming a partnership and

receiving pass-through tax treatment. The advantage of the corporate form was limited liability — the shareholders of a corporation are not responsible for its liabilities. By contrast, in a partnership, the partners are individually liable for the obligations of the business. Thus, one had to choose between limited liability and inferior tax treatment (the corporation), or unlimited liability and preferential tax treatment (the partnership). In 1977, Wyoming created a new type of business entity, the limited liability company (LLC) which combined aspects of the partnership and the corporation, and importantly conferred limited liability on all of the LLC owners. Most significantly, the IRS ruled in 1988 that the LLC could *elect* its tax classification, and naturally most LLC owners elect to have them treated as tax partnerships.[14] Thus, with the rise of the LLC, business owners could now obtain *both* limited liability *and* pass-through tax treatment.[15]

Because of this breakdown of the traditional logic of business taxation, and because of the shift to the use of pass-through entities by most business owners, New York would be wise to shift to taxing the entity level income of pass-through businesses. New York City already imposes such an entity-level tax, known as the Unincorporated Business Tax.

Two mechanisms exist that could be used to tax the profits of pass-through businesses. The first option, which seemingly exists in recognition of the distorted business tax environment, is the state's small filing fee on LLCs and partnerships based on gross income. The fee tops out at $4,500 annually for businesses with over $25 million in gross income. This filing fee could be redesigned as either a tax on a percent of gross receipts or as a tax on entity net income.

The second mechanism that could be used to tax pass-through businesses is New York's Pass-Through Entity Tax (PTET). This tax is a legacy of the federal limitation of the state and local tax deduction enacted as part of the federal 2017 tax law known as the "Tax Cuts and Jobs Act" (TCJA). The TCJA limited the federal income tax deduction for state and local taxes to $10,000, in effect raising taxes on wealthier residents of higher-tax states by multiple percentage points. In response to taxpayers' attempts to circumvent this limitation, the IRS ruled that the owners of pass-through businesses could elect to pay an entity-level tax to the state government, deduct that tax payment for federal income tax purposes, and then receive a credit against their personal income tax liability. In other words, the business owner would end up fully circumventing the SALT Cap and the state government would raise no additional revenue.

New York enacted a tax with this structure, the "Pass-Through Entity Tax" (PTET), and currently provides a rebate against the PIT for 100 percent of the tax. A 100 percent rebate is not necessary to incentivize payment of the tax, however, and Massachusetts and Connecticut both offer rebates around 90 percent of the entity-level tax paid. The value of the PTET is equal to a taxpayer's share of PTET paid multiplied by their federal income tax rate (37 percent for the highest earners). A taxpayer would therefore need to receive a rebate for at least 63 percent of PTET paid in order to not lose money in electing to pay the tax. In order to create an incentive to elect into the tax, and to account for partnership complexities, the rebate would likely need to be over 75 percent. Other states have noted this dynamic — for instance, Connecticut rebates only 87.5 percent of its Pass-Through Entity Tax.[16]

A 10 percent reduction in the PTET rebate would raise over $1 billion annually.

Revenue Proposal 5: Raise the Corporate Tax Rate

As part of the 2021 tax increases, the state's corporate franchise tax rate was increased for corporations with over $5 million in profits, from 6.5 percent to 7.25 percent. The increase was only temporary and scheduled to expire in 2023, which would have led to over a billion dollars in lost revenue annually.[17] The Executive Budget proposes to extend this rate for another 3 years. The state ought to end the practice of enacting temporary tax rate increases, which only create future fiscal cliffs. Further, there is plenty of room to continue raising the corporate tax rate.

Both the U.S. federal corporate tax rate and New York State's corporate tax rate have fallen steadily since the 1960s. The 2017 tax law known as the "Tax Cuts and Jobs Act" cut the U.S. federal corporate tax rate from 35 percent to 21 percent, bringing it to its lowest level since 1942.[18] New York State's corporate tax rate gradually fell from 8.5 percent in 2000 to a low of 6.5 percent in 2016 (under then-Governor Andrew Cuomo), the lowest rate since 1967. The corporate tax rate remained at its historic low of 6.5 percent until the 2021 tax increase.[19]

The corporate tax is New York's third largest source of tax revenue, behind the personal income tax and sales taxes. Due to the falling corporate tax rate over time, corporations now contribute a smaller percentage of the state's total tax collections than they did in prior decades. New York's corporate tax rate is also low by regional standards — New Jersey's rate is 11.5 percent; Pennsylvania's rate is 8.99 percent; and Massachusetts' rate is 8.0 percent.

Figure 3. New York's Falling Corporate Tax Rate: 1990 - 2024

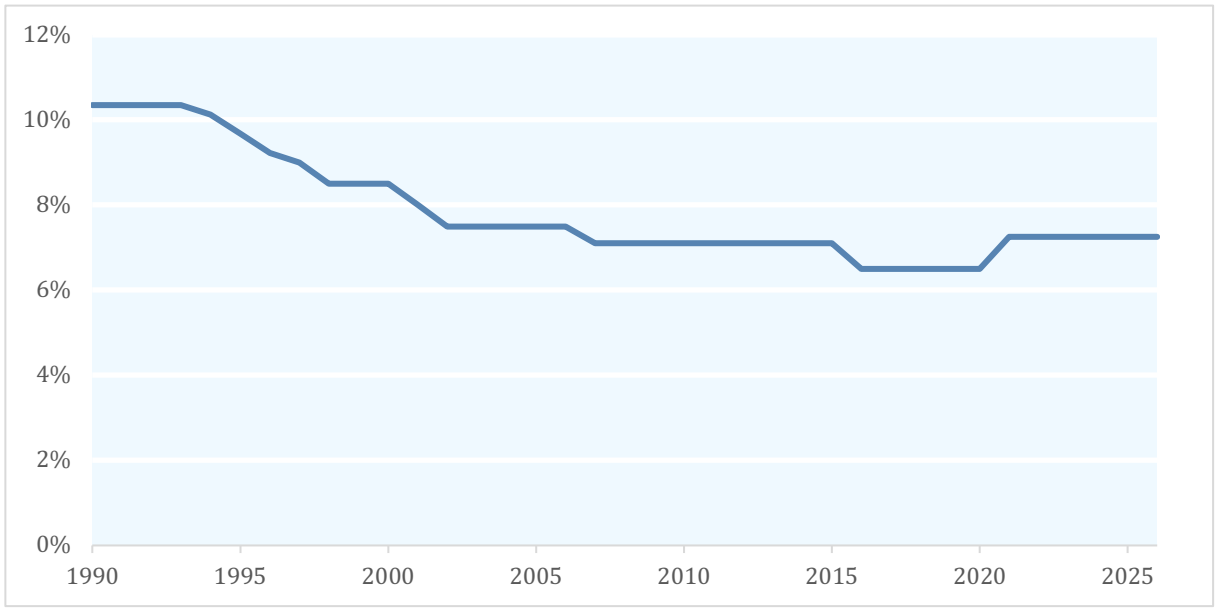
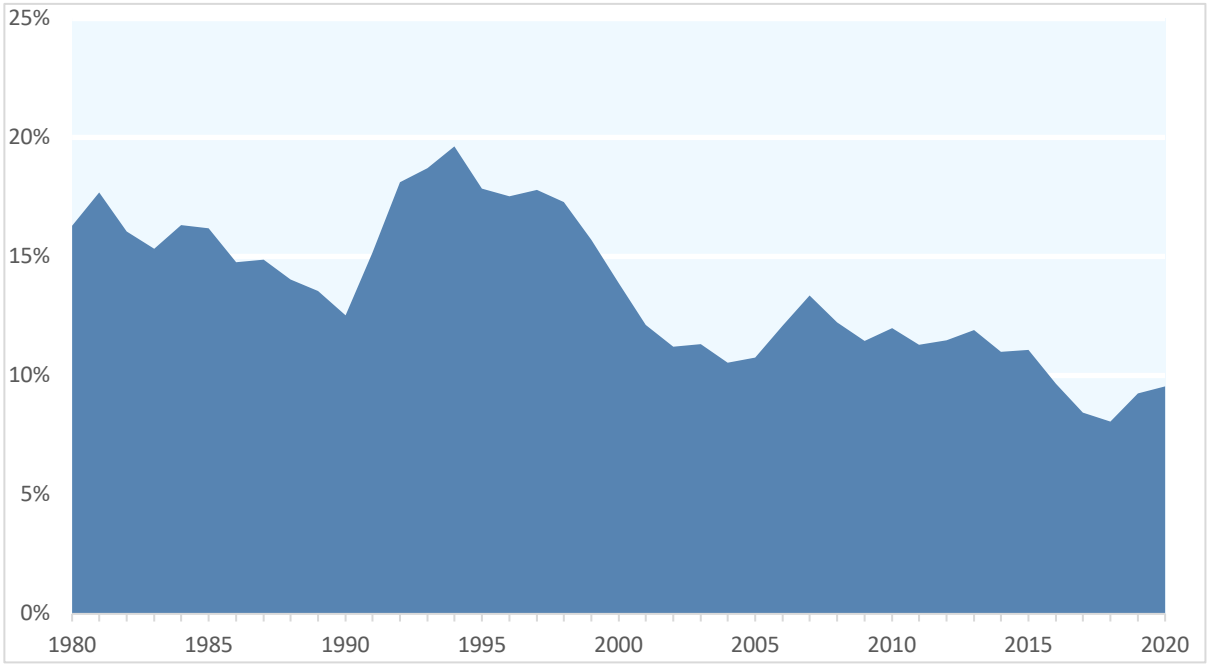


Figure 4. New York's Corporate and Business Tax Revenues as Share of Total Collections: 1980-2020



Revenue Proposal 6: Tax the Profit-Shifting of Multinational Corporations

A consistent focus of tax policy scholarship in recent decades has been the techniques used by multinational corporations to shift profits into low-tax foreign countries.[20] The 2017 federal tax legislation known as the "Tax Cuts and Jobs Act" (TCJA) enacted a provision that includes "global intangible low-taxed income" or "GILTI" in the taxable corporate income of U.S. corporations with overseas subsidiaries. The basic mechanic of the tax is that extranormal returns on tangible assets (defined as returns in excess of 10 percent of adjusted basis) are included in a corporate taxpayer's "GILTI" and thereby subject to U.S. tax. The theory is that such extranormal returns indicate the presence of high value intangible assets that were likely shifted out of the U.S. tax base into low-tax jurisdictions. A corporate taxpayer may then deduct 50 percent of GILTI, in order to account for the fact that profits shifted into foreign low-tax jurisdictions were like shifted out of other countries in addition to the U.S.

Leading tax law scholars recommend that states include GILTI in their tax base and include some amount of GILTI in the numerator of their apportionment factor.[21] New York currently exempts 95 percent of GILTI income from its corporate tax base, and apportions no GILTI income to New York. Corporate profits shifted out of the U.S. tax base necessarily rob state governments of revenue, and New York could substantially increase its corporate revenues by including some portion of GILTI in taxable income.

Including GILTI in the state tax base and apportioning some reasonable amount — say, New York's share of U.S. GDP — could raise $500 million to $1 billion annually.

Revenue Proposal 7: Reform the Estate Tax, or Tax Inherited Income

In principle, the estate tax should function as a tax on accumulated wealth at the end of an individual's life. However, it has largely ceased to perform this role due to a few unfortunate features of current estate tax law. Chief among them are that (i) the step up in basis rules eliminate taxable gain upon death, (ii) the estate tax exemption has continued to rise (currently, the first $26 million of a married couple's estate is exempt from federal estate tax, and the New York State estate tax exemption is over $13 million for a married couple), (iii) the wealthy can contribute their assets to a private foundation, thereby avoiding estate tax, and (iv) the estate tax planning industry has developed sophisticated tax avoidance techniques.

New York could reform any of the above features of its estate tax in order to more effectively tax accumulated wealth at death. The easiest strategy would be to end step-up in basis at death for state tax purposes. Or, it could shift to a new, simpler inheritance tax scheme whereby inherited income is included in the recipient's income, putting it on par with wage income and investment income.[22]

Revenue Proposal 8: Enable a Direct Wealth Tax

Finally, New York could seek to impose an annual tax on the total wealth of the ultra-rich. According to the Institute on Taxation and Economic Policy, a 3 percent tax on wealth held above $30 million in New York would raise $134.4 billion, greater than the entire New York State operating budget in fiscal year 2023.[23] The same rate on wealth held above $1 billion would raise $13.2 billion.

Because a wealth tax would likely incentivize top holders to adopt tax avoidance strategies, a lower rate applied to a broader base would perform better than a higher rate on a narrower base. For New York, nearly $6 trillion of wealth is held by ultra-rich households that are not billionaires.[24] Given that this group contains nearly 30 thousand households — rather than 78 billionaires — it makes for a sounder base for a potential wealth tax.

A state level wealth tax does face one considerable obstacle to implementation. The New York State Constitution prohibits a direct wealth tax, so a constitutional amendment would be necessary.

Expenditure Proposal 1: Reform the Empire State Child Credit

In addition to raising revenue, the tax law is an important tool for poverty relief policy. New York State annually spends about $1.4 billion combined on the Earned Income Tax Credit and the Empire State Child Credit (ESCC). The ESCC itself costs about $600 million annually, and provides $330 per child — but notably excludes children under the age of 4, for no discernible policy reason. Families are eligible for the ESCC if they have income over $3,000 and under $110,000 (or $75,000 in the case of a single filer).

The state should act to eliminate the carve-out from the Empire State Child Credit for children under 4, include filers who use an individual taxpayer identification number (ITIN) in the scope of the credit (so as to include undocumented immigrants), and eliminate the phase-in that leaves out very low income earners. The proposed "Working Families Tax Credit," in particular would make many of the necessary reforms to expand state poverty relief to the poorest New Yorkers, while simplifying the administration of the credit. The estimated cost for these reforms is about $300 million.

Expenditure Proposal 2: Decouple from Qualified Opportunity Zones

The 2017 federal tax legislation known as the Tax Cuts and Jobs Act included a provision creating tax benefits for investments in "Qualified Opportunity Zones" (QOZs). In principle, QOZs were intended to direct investment into depressed areas by providing tax benefits. In reality, they have been plagued with the predictable problems that business tax incentives commonly face. New York partly decoupled from the QOZ rules, but due to what appears to be a technical drafting error did not complete the decoupling process.[25]

Taxpayers can receive three federal benefits by investing in QOZs:

(1) Taxes may be deferred on capital gains that are reinvested in a QOZ until the earlier of (i) when the property is sold or exchanged or (ii) the end of 2026.
(2) Taxes on capital gain deferred above in (1) can be reduced by 10 percent or 15 percent if the investment is held for 5 years or 10 years (respectively);
(3) If the investment in a QOZ is held for at least 10 years, all of the gain is tax-free.

To take a concrete example, suppose a taxpayer invested $100,000 in the stock market and that investment is now worth $1 million — of which $900,000 would be taxable gain if the stock were sold. If the taxpayer liquidates her holdings and invests that $1 million in a QOZ, she can defer paying tax until she sells the property. If her $1 million investment grows to $2 million ($1.9 million of which would be taxable gain in this example), and she holds onto her investment for 10 years, she owes no federal income tax when she ultimately sells.

The Urban Institute conducted 70 interviews with QOZ investors and found that the program had generally not been effective in meeting its stated goal of promoting investment in depressed areas.[26] Investors will naturally be drawn to projects with the highest rate of return, favoring large commercial developments over small business or affordable housing. Moreover, the 10 year investment period required to get the full tax benefit discourages investments in riskier areas. The New York Times reported in depth on the many ways in which these investments do nothing to support the impoverished communities for which the program was ostensibly intended. [27]

New York budget legislation for fiscal year 2022 decoupled from benefits (1) and (2) above, but not (3), meaning that an investor's gains from a QOZ could be entirely tax free, if held for ten years,

Expenditure Proposal 3: Reform Industrial Development Agency Tax Breaks

The state's network of Industrial Development Agencies (IDAs) are empowered to provide tax breaks to businesses. As of 2019, the net value of these tax breaks was estimated by the Office of the State Comptroller's office to be nearly $1 billion.[28] A recent analysis by Greg LeRoy and Christine Wen of Good Jobs First shows that in 2021, public schools lost over $1.8 billion in funding, much of which was attributable to IDA-related tax breaks.[29]

All such tax breaks narrow the tax base and force other taxpayers to bear the burden of higher rates. In the absence of clear and compelling evidence that the state receives a net fiscal benefit from business

subsidies, these tax breaks should be avoided. Further, there is a widespread academic consensus that business tax incentives are ineffective at promoting economic development.

[1] For a journalistic account of broad-based, progressive tax reform in global perspective, see T. R. Reid, *A Fine Mess* (Penguin Press, 2017).

[2] Meg Wiehle et al. "Who Pays? A Distributional Analysis of the Tax Systems in all 50 States: Sixth Edition" *Institute on Taxation and Economic Policy* (October 2018), itep.org/whopays/.

[3] New York State Department of Taxation and Finance, "Personal Income Tax Filers, Summary Dataset 3 - Statewide Major Items and Income & Deduction Components by Liability Status and Detail Income Range: Beginning Tax Year 2015" (accessed October 2022), data.ny.gov/Government-Finance/Personal-Income-Tax-Filers-Summary-Dataset-3-State/rt8x-r6c8.

[4] All rates are for joint return filers. New York State Department of Taxation and Finance, "2020 personal income tax forms: IT-201-I" and past editions (accessed October 2022), tax.ny.gov/forms/prvforms/income_tax_2020.htm.

[5] Revenue estimate by the Institute on Taxation and Economic Policy (ITEP).

[6] Revenue estimate by ITEP.

[7] Revenue estimate by FPI.

[8] Long-term capital gains are additionally subject to the Net Investment Income Tax ("NIIT") of 3.8 percent for married couples with modified adjusted gross income in excess of $250,000. The NIIT applies to capital gains, interest, dividends, rents and royalties, as well as other types of investment income, and was enacted as part of the 2012 Patient Protection and Affordable Care Act.

[9] Estimates by ITEP.

[10] https://www.propublica.org/article/billionaires-tax-avoidance-techniques-irs-files

[11] For years in which the individual's portfolio loses value overall, such losses could be carried into prior or future years to offset gains, thus achieving fair tax treatment of their real economic income over time.

[12] Brian Galle, David Gamage, Darien Shanske, "Solving the Valuation Challenge: The ULTRA Method for Taxing Extreme Wealth", *Duke Law Journal* (forthcoming 2023), available at papers.ssrn.com/sol3/papers.cfm?abstract_id=4036716.

[13] As of 2014, 95 percent of businesses were organized as pass-through entities. Aaron Krupkin and Adam Looney, "9 facts about pass-through businesses" *Brookings Institute* (May 15, 2017) brookings.edu/research/9-facts-about-pass-through-businesses.

[14] IRS Revenue Ruling 88-76.

[15] Savvy readers will note that there is also the option of the S-Corporation, which predates the LLC, and is also a pass-through entity for tax purposes. The requirements for owning an S-Corporation were initially quite restrictive, and remain considerably more restrictive than the rules that apply to LLCs. In both cases, over the last 30 years, the rules have changed to make it considerably easier to obtain limited liability as well as entity-level tax benefits.

[16] https://portal.ct.gov/-/media/DRS/Forms/2022/Pass-Through/CT-1065-CT-1120SI-Instructions_1222.pdf

[17] FPI estimate.

[18] https://www.taxpolicycenter.org/laws-proposals/major-enacted-tax-legislation-1940-1949.

[19] The corporate tax increase was enacted only for tax years 2021 through 2023.

[20] See, e.g., Joseph Bankman, Mitchell A. Kane, Alan O. Sykes, "Collecting the Rent: The Global Battle to Capture MNE Profits" in *Tax Law Review*, vol. 2. No. 2 (Spring 2019).

[21] Darien Shanske and David Gamage, "Why States Can Tax the GILTI" 91 State Tax Notes 967 (2019), at https://www.repository.law.indiana.edu/facpub/2745/; Darien Shanske and David Gamage, "Why States Should Tax the GILTI," 91 State Tax Notes 751 (2019), at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3374987.

[22] For an extended analysis of the benefits and mechanics of an inheritance tax, see Lily L. Batchelder, "Leveling the Playing Field between Inherited Income and Income from Work through an Inheritance Tax", *NYU Law and Economics Research Paper Series* (February 2020), available at papers.ssrn.com/sol3/papers.cfm?abstract_id=3526520.

[23] Carl Davisd, Emma Sifre, Spandan Marsini, "The Geographic Distribution of Extreme Wealth in the U.S.", *Institute on Taxation and Economic Policy* (October 13, 2022) available at https://itep.org/the-geographic-distribution-of-extreme-wealth-in-the-u-s/#appendix-e.

[24] ITEP Report.

[25]See Part DDD, S2509C at https://www.nysenate.gov/legislation/bills/2021/S2509. Note that the legislation adds back gain excluded under section 1400Z-2(a)(1)(A) of the Internal Revenue Code but does not add back gain excluded under section 1400Z-2(a)(1)(C) (which provision excludes gain on investments held for 10 years).

[26] Brett Theodos, Jorge Gonzalez-Hermoso, Brady Meixell, "The Opportunity Zone Incentive Isn't Living Up to Its Equitable Development Goals." (June 17, 2020) at: https://www.urban.org/urban-wire/opportunity-zone-incentive-isnt-living-its-equitable-development-goals-here-are-four-ways-improve-it

[27] https://www.nytimes.com/2019/08/31/business/tax-opportunity-zones.html

[28] https://www.osc.state.ny.us/press/releases/2022/06/dinapoli-releases-annual-ida-report

[29] https://goodjobsfirst.org/wp-content/uploads/2023/02/How-Tax-Abatements-Cost-New-York-Public-Schools.pdf

Long-Term Trends: State Fiscal Policy from the Great Financial Crisis through COVID-19

New York's Lost Fiscal Decade, 2008 – 2019

The fiscal policy pursued in the 2010s left many public services, including social welfare and support for local governments, smaller than they were prior to the recession

The financial crisis that began in 2007 posed immense challenges for U.S. states. Faced with plummeting revenues, many states enacted budget cuts that deepened an already severe recession. How states balanced their budgets, however, and supported economic recovery was a matter of policy choice. In the wake of its recessionary cuts, New York State embarked on a decade of fiscal retrenchment. The fiscal policy New York pursued in the 2010s left many public services, including social welfare and support for local governments, smaller than they were prior to the recession. The result was halting and uneven economic recovery characterized by high inequality and economic and regional polarization. As revenue began to rebound, the state implemented tax cuts and tax credits for corporate taxpayers, and adhered to strict spending limits rather than reinvesting in core public services. This decade of fiscal stagnation left the state unusually fiscally and economically exposed to Covid crisis. This section examines state fiscal policy over the 2010s, using pre-recession budgets as a baseline to compare changes over a decade of economic recovery.

2008 Recession Onward: A Decade of Reduced Spending

The U.S. entered a recession in December 2007, although it would take more than a year for its severity to become apparent. A financial crisis had been unfolding over the course of 2007, as cracks began to appear in the country's housing market and financial system. Slowing investment and falling asset prices were enough to bring economic growth to a halt even before 2008 delivered a series of systemic shocks to the global financial system that created the worst economic downturn since the Great Depression.

The U.S. unemployment rate rose steadily through late 2007 and 2008. Between November 2007 and September 2008, unemployment rose from 4.7 percent to 6.1 percent.[1] Rather than reaching a peak, however, the financial crisis deepened in fall 2008. In September, investment bank Lehman Brothers declared bankruptcy, exacerbating an already devastating capital markets liquidity crisis. The financial crisis began to take a greater toll on the real economy. Over the following six months, rising unemployment accelerated, reaching 9.5 percent by June 2009 before peaking at 10 percent four months later. Growth in gross domestic product (GDP) turned negative in the third quarter of 2008 and did not resume growth until the third quarter of the following year.[2] By June 2009, the country had lost 7.4 million jobs. Inflation-adjusted GDP returned to pre-recession levels in the fourth quarter of 2010. Employment only returned to its former peak in May 2014.[3]

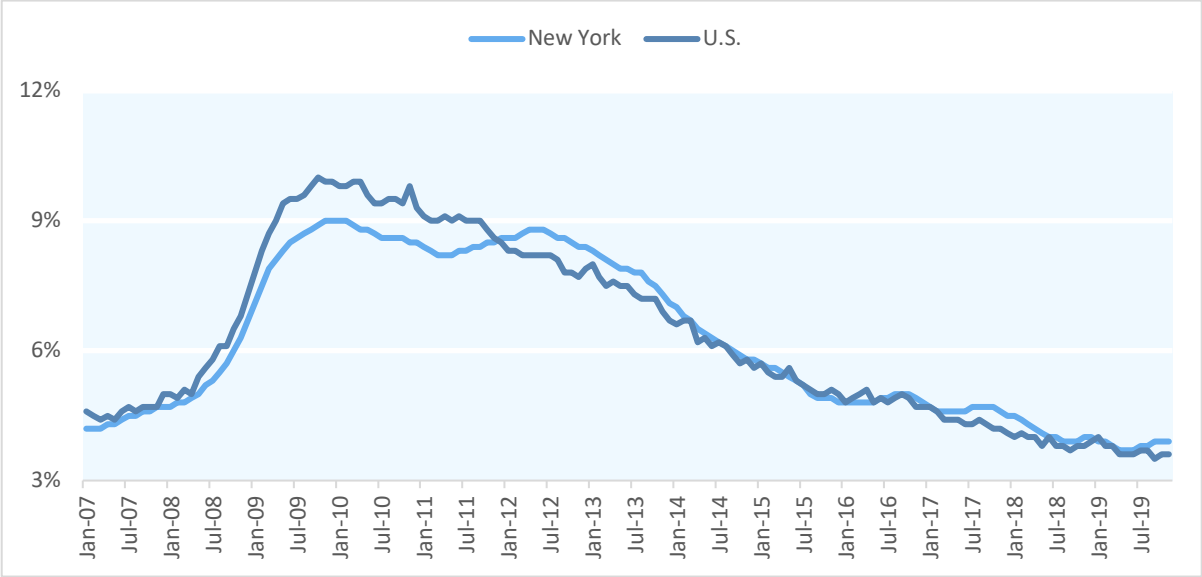
As the severity of the recession began to become apparent, New York lawmakers took emergency measures to stabilize the state's finances. The state's unemployment rate was rising in lockstep and its economy likely contracted earlier than that of the U.S., given the initial fallout in the financial sector.[4] Tax revenues began to deteriorate continuously throughout the year. In the governor's fiscal year 2009 executive budget, the state's Division of Budget initially believed recession would be avoided.[5] By the middle of the fiscal year, the state had implemented a $2.8 billion savings plan in the enacted budget financial plan, a further $630 million in the first quarter update, and a further $427 million approved in an emergency legislative session in August.

Despite these efforts, which slashed funding to Medicaid, local aid, and reduced the size of the state workforce, the state still faced a $1.5 billion current-year gap in fiscal year 2009. State operating spending ended about $2.3 billion, or 2.9 percent, lower than planned in the enacted budget.

While fiscal year 2009's $2.2 billion budget gap could be managed through ad hoc spending restraint, as the economy began to reach its bottom and revenue continued to plunge, the following year's gaps grew to $17.9 billion. A three-pronged approach closed the fiscal year 2010 gap: lawmakers enacted a $6 billion spending cut (mainly affecting healthcare, school tax relief, and school aid); raised income tax rates on high earners to bring in $5.3 billion; and benefited from $4.9 billion in federal aid.[6]

Legislators' efforts were sufficient to stabilize the New York State budget. After falling in fiscal years 2009 and 2010, after adjusting for inflation, revenue was bolstered by newly progressive income tax rates and a nascent economic recovery. While state revenue rebounded in fiscal year 2011, fiscal pressure on local governments continued. Together with inadequate federal stimulus and a lack of new investment from the state, fiscal retrenchment resulted in a slow and uneven economic recovery. While the U.S. recovery moved forward, New York veered toward a "double-dip" recession. By the middle of 2011, the state's unemployment rate began climbing continuously for the next 12 months. The state's GDP growth ground to a halt in 2011. This economic setback largely fell on low-income workers already hit hardest by the recession's first wave. The fiscal retrenchment during which this backstep occurred was not a budgetary necessity, but a policy choice.

Figure 1. Unemployment rate for New York and the U.S., 2007 to 2019



Spending Trends in 2010s: The State Role in Public Life Shrinks

State spending remained constrained through the decade, rather than following economic growth upward

Public investment is essential to stimulate the economy during economic downturns. Stimulus can take the form of new public works projects that employ dislocated workers, funding for public assistance to support households facing loss of income, or, less effectively, tax cuts. Such stimulus creates jobs and boosts consumer spending and investment, lifting economic growth.[7]

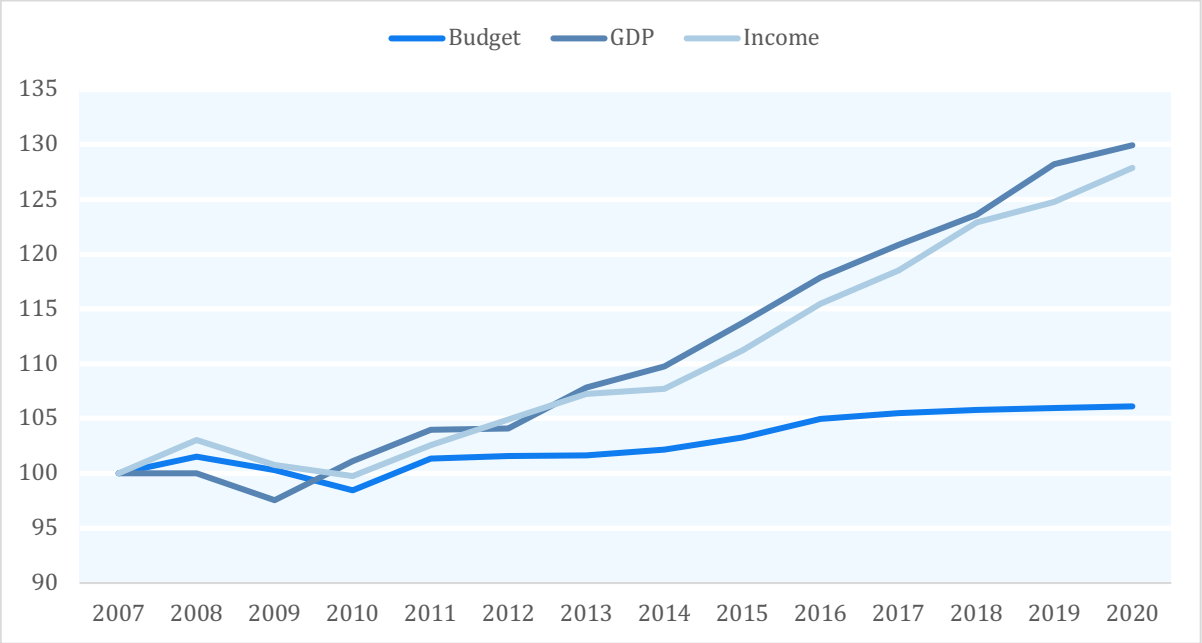
In the wake of the 2007-08 financial crisis, the state largely took the opposite approach, cutting its way to balanced budgets. In the acute phase of the crisis, the state relied on spending cuts, federal aid, and, to a lesser extent, temporary tax increases to close gaps created by the recession. In the recovery managed by Governor Cuomo, the state aggressively restrained spending, in many cases never restoring funding for key public services to pre-recession levels.

As the economy began to recover, itself slow by historic standards, state spending remained constrained through the following decade, rather than following economic growth upward. This left the state a structurally smaller part of public life than it had been prior to the recession. By fiscal year 2020, state operating funds spending was just 6.1 percent higher than its level in fiscal year 2007, after adjusting for inflation. By contrast, state GDP and personal income were 29.9 percent and 27.9 percent larger, respectively. Both of these measures, income and economic output, grew more than five times as quickly as state spending.

Figure 2. State operating funds spending, GDP, and personal income, fiscal years 2007 to 2020

Income and economic output grew more than five times as quickly as state spending

Indexed to 2007 (adjusted for inflation)

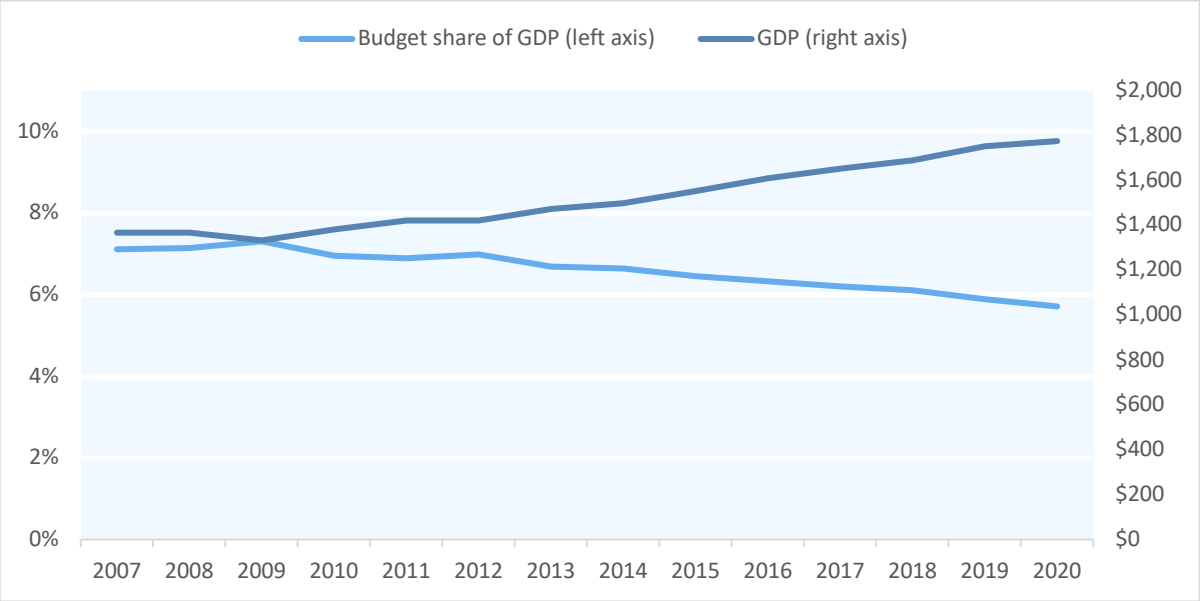


During the 2007-09 recession and its long aftermath, New York's public sector declined in relation to the state's economy. Between fiscal years 2007 and 2020, state spending had declined from 7.1 percent of GDP to 5.7 percent; its share of income fell from 9.1 percent to 7.5 percent.[8] This divergence illustrates the state's policy priorities in the 2010s. The state's fiscal capacity — its ability to raise resources to meet the state's needs — expanded far faster than its spending. The state's slow growth during this period was not an economic necessity, but a policy choice. Rather than restore funding cut during the acute phase of the crisis, or expand services in areas of mounting social strain, including childcare and housing, the state restrained spending. As revenue continued to grow alongside the economy, the state restrained spending by cutting taxes and expanding tax breaks, primarily to the benefit of corporate taxpayers.

Figure 3. New York GDP and state spending as a share of GDP, fiscal years 2007 to 2020

Between FY 2007 and 2020, state spending declined from 7.1 percent of GDP to 5.7 percent

2020 dollars



Areas of Spending Growth, 2007-2020: Medicaid and Education

New York's budget growth was restrained on an ongoing basis through the 2010s. Beginning in fiscal year 2013, annual state spending growth was constrained to a self-imposed two percent target set by Governor Cuomo. While the limit was occasionally breached — and obfuscated by fiscal gimmicks — spending growth between fiscal year 2013 through 2021 did average 2.0 percent. Accounting for inflation, the budget's annual rate of growth was just 0.5 percent under Governor Cuomo.

More than half of New York's state spending is accounted for by two spending programs: Medicaid and support for primary and secondary education. Together, these two policy areas accounted for 54 percent of the state operating budget in fiscal year 2020. School aid comprised a relatively consistent share of state spending: 26 percent of the budget in fiscal year 2007 rising to 29 percent in fiscal year 2020. Medicaid, however, facing the sustained cost pressure buffeting the U.S. healthcare sector, rose from 17 percent to 23 percent of state spending over the same period.

Medicaid

New York's Medicaid spending has risen in line with that of the U.S. as a whole

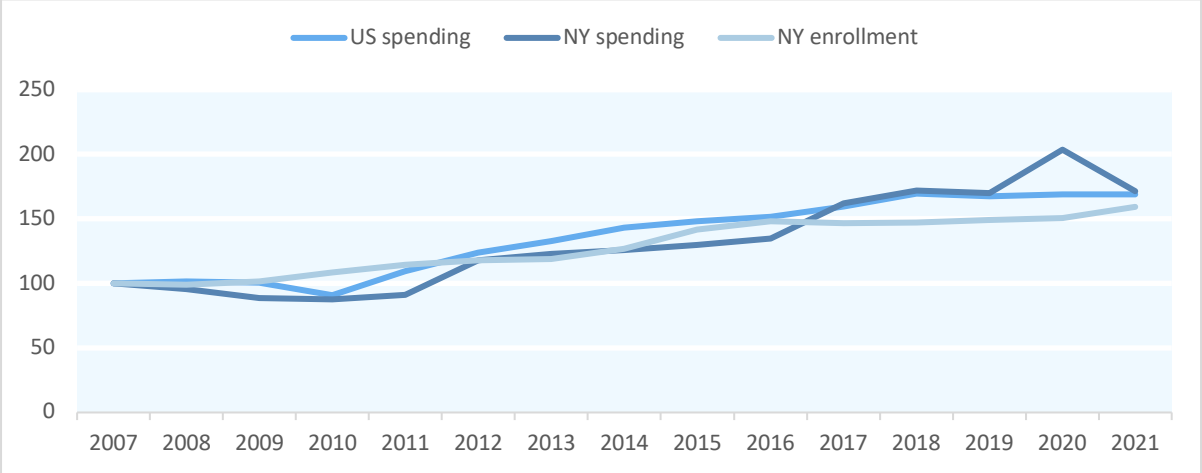
New York's rising Medicaid costs were driven both by nationwide cost pressures endemic to the healthcare sector, and by rising Medicaid caseloads. Between fiscal years 2007 and 2019, state Medicaid spending rose 70 percent. Collective state spending for all U.S. states rose 67 percent over the same period.[9] New York's Medicaid caseloads rose 49 percent.

New York's rising caseload was driven initially by the recession, which lowered income and increased unemployment, pushing workers from private insurance to Medicaid. Changes to eligibility criteria made more New Yorkers eligible for Medicaid and, beginning in 2014, the Affordable Care Act (ACA) expanded coverage for low-income adults.[10] Rising Medicaid enrollment over this period cut the state's rate of healthcare uninsurance in half.[11] Cost increases over the second half of the decade were attributable to nationwide healthcare cost inflation. Medicaid enrollment was stable between 2016 and 2020, and the ACA increased federal support for the state program, helping the state carry its expanded caseload. Over the entire period, New York's Medicaid spending has risen in line with that of the U.S. as a whole, as healthcare costs have risen faster than inflation.

Figure 4. U.S. and New York Medicaid spending and New York enrollment

New York's Medicaid spending has risen in line with that of the U.S. as a whole

Indexed to 2007



Education

In the aftermath of the 2007-09 recession, school aid became the focus of spending reductions

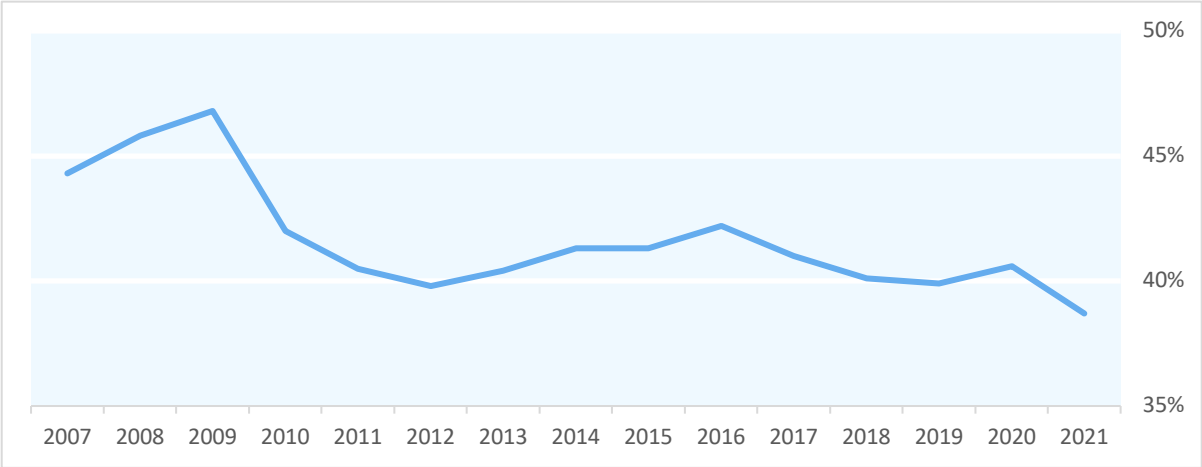
New York's Medicaid program accounted for 45 percent of state spending increase between fiscal years 2007 and 2020. State aid for elementary and secondary school accounted for a further 38 percent of spending increase over the same period. Despite its lower pace of growth, school aid's fiscal dominance meant even its modest pace of growth plays an essential role driving spending. In the aftermath of the 2007-09 recession, school aid became the focus of spending reductions. School aid was cut in fiscal years 2010 through 2012, and, after adjusting for inflation, did not return to pre-recession funding levels until fiscal year 2016.

The level of school aid has been contested in a series of legal challenges mounted by the Campaign for Fiscal Equity over the last three decades. In 2003, New York courts ruled that the state's constitution required it to provide students a "sound basic education." Four years later, the state adopted a school funding formula, referred to as foundation aid, and agreed to phase in legally-required and formula-based school

funding over a four year period. The four year phase in was initially interrupted by the recession. In the following recovery, the state slowed the pace of annual school aid increases and continued to fall short of full foundation aid funding levels until fiscal year 2024.[12]

To restrain costs associated with Medicaid and school aid, lawmakers enacted statutory caps on program spending. In fiscal year 2012, Governor Cuomo introduced a cap on Medicaid spending, limiting annual growth to no higher than the ten-year average annual rate of the medical component of the consumer price index. School aid was limited to the growth rate of personal income in New York State. These spending caps were expected to save the state $7.0 billion immediately, rising to $14.3 billion by fiscal year 2015.[13] Because school aid was subject to the deepest cuts in the aftermath of the recession, this cap was imposed at its funding nadir. School aid's slow subsequent growth has generally followed that of the overall budget. The cap has also shifted the burden of school funding toward local governments, increasing fiscal strain imposed by the state.[14] Local school costs outpaced state aid over this period, lowering the state's share of total school costs from 44.3 percent in school year 2006-07 to 38.7 percent in school year 2020-21.[15]

Figure 5. State share of total school spending, school years 2006-07 to 2020-21



Spending Cuts

Between fiscal years 2007 and 2020, state spending outside Medicaid and school aid fell 11 percent, after adjusting for inflation

The state's fiscal stagnation over the course of decade, together with the fiscal dominance of its largest two spending areas, left little remaining fiscal room. Large swathes of the state budget saw funding levels cut or static funding continually eroded by inflation. Between fiscal years 2007 and 2020, state spending outside Medicaid and school aid fell 11 percent, after adjusting for inflation.

Funding cuts were distributed across programmatic areas supported by the state budget. These cuts were generally focused on the state's principal type of spending: grants to local governments. Much of the state's spending, including its two largest expenditures — Medicaid and school — as well as a range of social welfare and mental health programs, is passed to local governments, which directly administer the programs. This funding may be tied to programs' caseloads, or disbursed by the state as fixed-level grants.

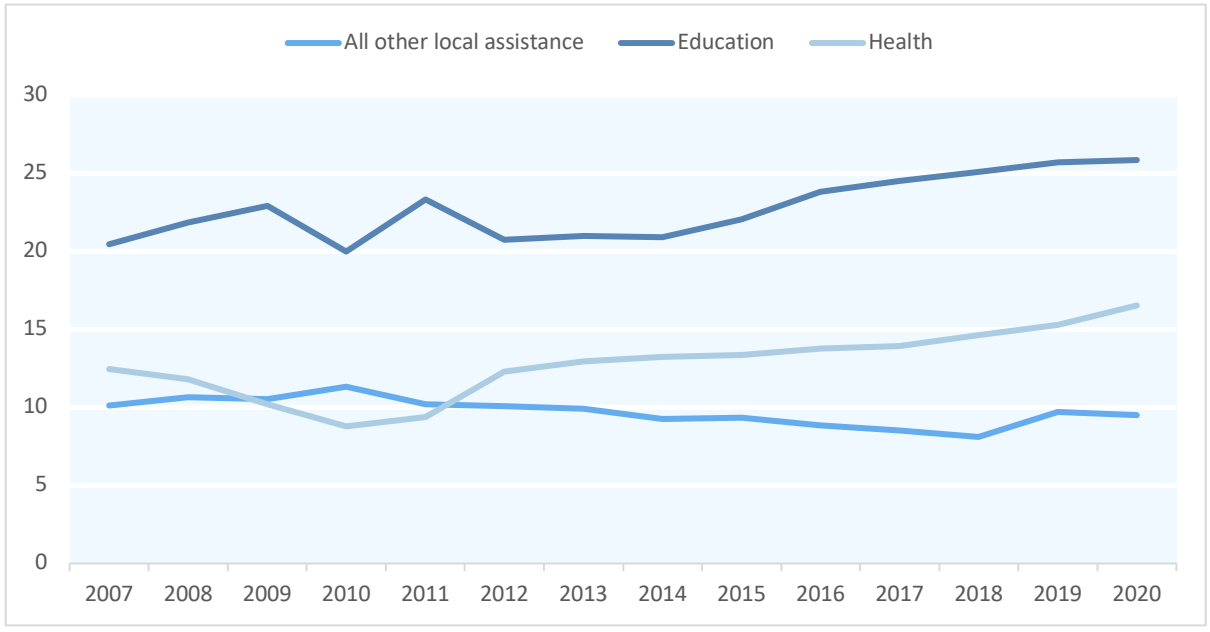
As such, reductions in local assistance in some cases may be tied with declining usage of the program being funded. In other cases, falling funding is unrelated to underlying local need.

In addition to this program-based local funding across the state budget, the state provides municipalities with unrestricted financial support (referred to in the figure below as local government assistance). The majority of this spending is disbursed through the state's Aid and Incentives to Municipalities (AIM) program.

Beyond funding for health and education programs (primarily for Medicaid and school aid, respectively), collective state assistance to local governments fell 6 percent between fiscal years 2007 and 2020. These budget cuts, together with state-imposed restrictions on local governments' ability to raise revenue, shifted much of the burden of the state's self-imposed fiscal restraint in the 2010s onto local governments across New York State. This funding shift constrained local governments' ability to maintain or expand services in response to local needs.

Figure 6. Health, education, and all other local government assistance, fiscal years 2007 to 2020

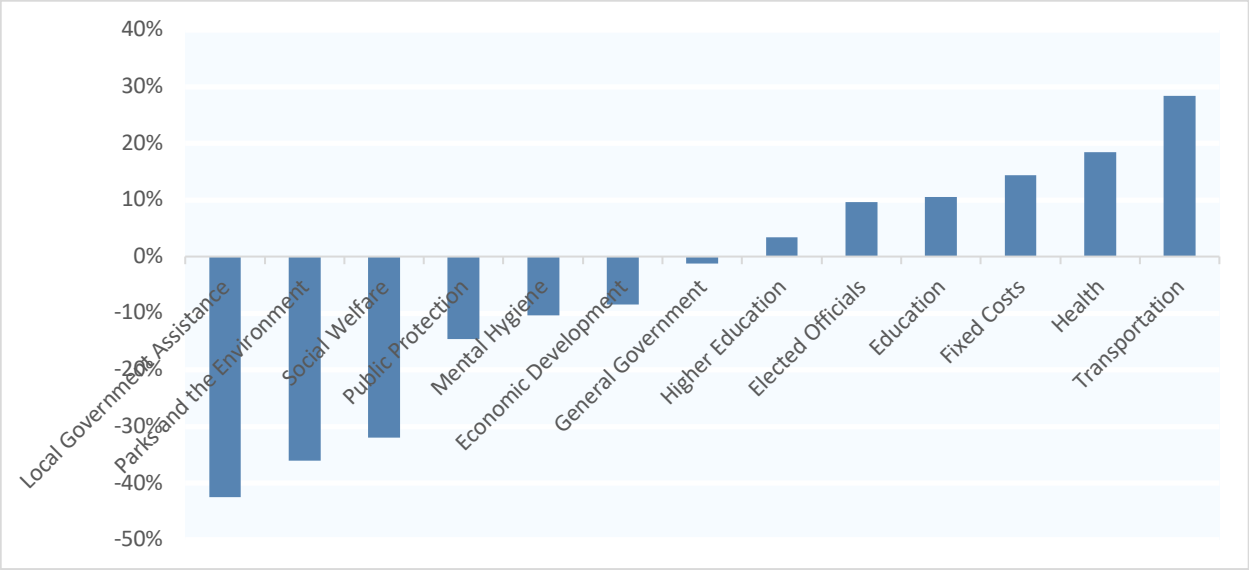
2020 dollars in billions



New York's social welfare agencies faced the largest budget cuts in absolute terms between fiscal years 2007 and 2020, with state funding falling by $1.4 billion per year, after adjusting for inflation. Unrestricted local government assistance fell the farthest in percentage terms (down $558 million — 42.4 percent) over the same period. Before delving into these critical areas in detail, it is important to note cuts in three additional areas: mental hygiene, environmental protection, and public protection.

Figure 7. State spending change by programmatic area, fiscal years 2007 to 2020

Adjusted for inflation



Spending cuts to the mental hygiene programmatic area consisted primarily of significant cuts to two offices: Office for People with Developmental Disabilities, which fell 20 percent, and Office of Addiction Services and Supports, which fell 12 percent. Like social welfare cuts, spending reductions to these offices were focused on their largest expenditure: grants to local government. Across the state, local public assistance administrations experienced consistently declining support from a range of state funding sources over the 2010s.

Each of the two major state agencies that comprise its parks and environment programmatic area faced 35 percent inflation-adjusted cuts between fiscal years 2007 and 2020. The larger Department of Environmental Conservation (DEC) saw its budget fall by $144 million, while the Office of Parks, Recreation, and Historic Preservation $93 million. Parks cuts were largely focused on state operations personal services–indicating permanent state staffing reductions. DEC faced across-the-board cuts to its operating funds as well as its special revenue funds, which are dedicated to specified program areas, indicating broad spending reductions on land, wildlife, and marine conservation, waste remediation, climate adaptation, and other management and regulatory activities.

New York's falling prison population led to lower spending on public protection and criminal justice. The programmatic areas largest spending category, corrections, saw funding fall 8 percent. This was driven by, but less than, the 27 percent decline in the state prison population between 2008 and 2019.[16]

Social Welfare

Falling support for public assistance reflects the state's decade-long effort to shift social welfare responsibilities from the state to local governments

The state's social welfare spending is dominated by local government grants disbursed by two state agencies: the Office of Temporary and Disability Assistance (OTDA) and the Office of Children and Family Service (OCFS). These grants fund a range of public assistance programs, chiefly the state-funded portion of the federal Temporary Assistance for Needy Families (TANF) program. State TANF funding supports a range of public assistance programs, including cash assistance for low-income households, work support and training programs, and child welfare programs. A portion of these funds also finance the state's supplement to the earned income and child tax credits.

Local government assistance disbursed by the state's two primary social welfare agencies fell during the 2010s. Between fiscal years 2007 and 2020, local government grants disbursed by OTDA fell 28 percent, after adjusting for inflation. Over the same period, OCFS local assistance was flat, after adjusting for inflation.[17] Falling support for public assistance reflects the state's decade-long effort to shift social welfare responsibilities from the state to local governments.

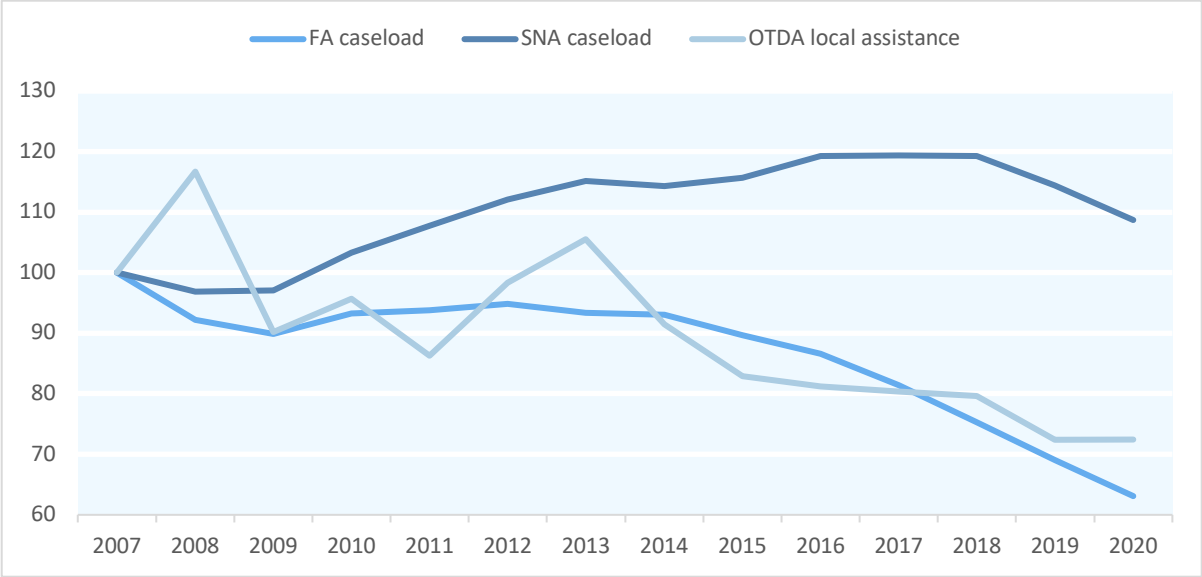
In fiscal year 2012, the state changed public assistance financing to shift costs to local governments. The state shifted funding for Family Assistance (FA) cases, which meet federal TANF requirements, from shared between local, state, and federal sources entirely to the federal block grant. This relief for local governments was counterbalanced by an increase in the local share of funding for Safety Net Assistance (SNA). SNA provides the state-funded benefits to cases not eligible to FA, including single adults, families without, and families that have reached the federally-imposed time restriction on cash assistance. In fiscal year 2012, the state shifted SNA funding from a 50 percent-50 percent split between the state and local governments to 29 percent state-funded and 71 percent locally-funded.[18]

While this funding change had little immediate effect on local public assistance budgets, it has substantially raised their costs over subsequent years. Because SNA is less restrictive than FA, they have tended to rise over time as the more restrictive FA cases have fallen. Between fiscal years 2007 and 2020, the state's SNA caseload rose 9 percent while its FA caseload fell by 37 percent.[19]

The state also reduced its support for other elements of the state-funded TANF program. Between fiscal years 2010 and 2020, the state reduced its support for local public assistance administration by more than $100 million, after adjusting for inflation, a 40 percent cut.[20] Further funding shifts were made to a series of childcare and other social welfare programs.[21] These changes have reduced the state's spending on social welfare. This is not the result of a falling level of social need in New York State, but of the state's efforts to shift the fund obligations to local governments.

Figure 8. State OTDA spending and FA and SNA caseloads, fiscal years 2007 to 2020

Indexed to fiscal year 2007



Local Governments

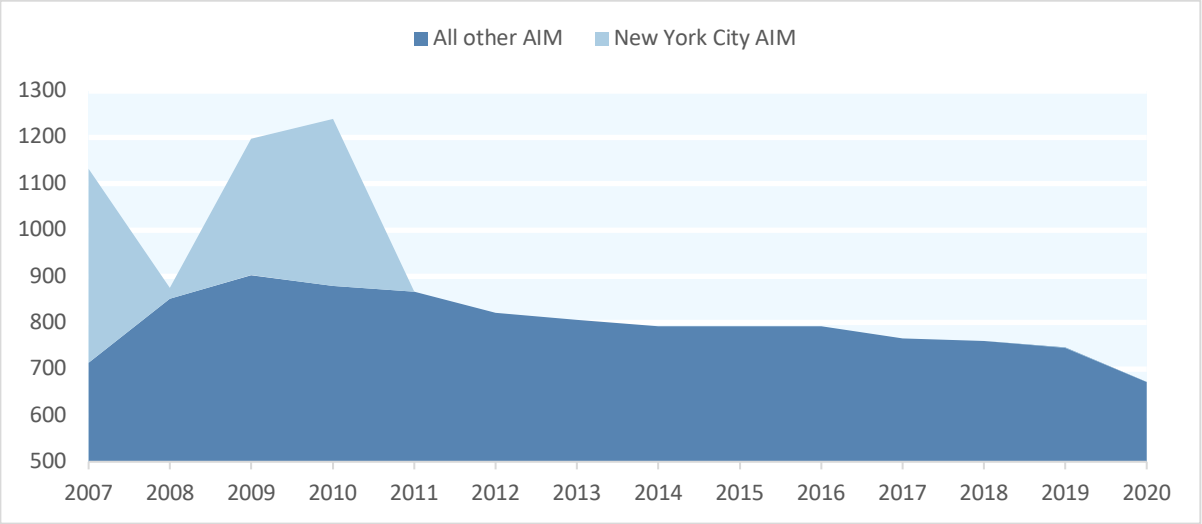
Between fiscal year 2007 and 2020, aid and incentives for municipalities funding fell 41 percent, after adjusting for inflation

Aid and incentives for municipalities (AIM), which accounts for the vast majority of spending in the state's local government assistance program area, provides unrestricted fiscal support for local governments. Between fiscal year 2007 and 2020, AIM expenditures fell 41 percent, after adjusting for inflation. Most of these cuts were made in the aftermath of the 2007-09 recession. In fiscal year 2011, AIM funding was cut by $373 million — 31 percent — after adjusting for inflation. Most of this cut resulted from the complete elimination of AIM for New York City.[22]

For the ensuing decade, funding was held flat, not indexed to inflation. Further cuts to AIM came in fiscal year 2020, when aid to towns and villages was eliminated, a 10 percent cut, after adjusting for inflation.[23] Local government cuts have tightened state-imposed fiscal constraints on localities, which have limited capacity to raise revenue on their own.

Figure 9. AIM funding to New York City and all other local governments, fiscal years 2007 to 2020

2020 dollars in millions



Falling state financial support for local governments has not coincided with falling local financial responsibilities. Rather, mandatory local government contributions to state-managed programs accounted for the vast majority of local government revenues. A 2019 report from the New York State Association of Counties documented nine state-controlled spending mandates that collectively accounted for more than 90 percent of local governments' property tax revenue.[24] This funding strain was compounded by the 2011 property tax cap, in which the state limited local property tax growth from exceeding two percent per year. Taken together, the shifting of funding for core public services from the state to local government and restriction of local governments' ability to raise revenue has dramatically increased local fiscal constraints, curtailing their flexibility and ability to respond to local needs.

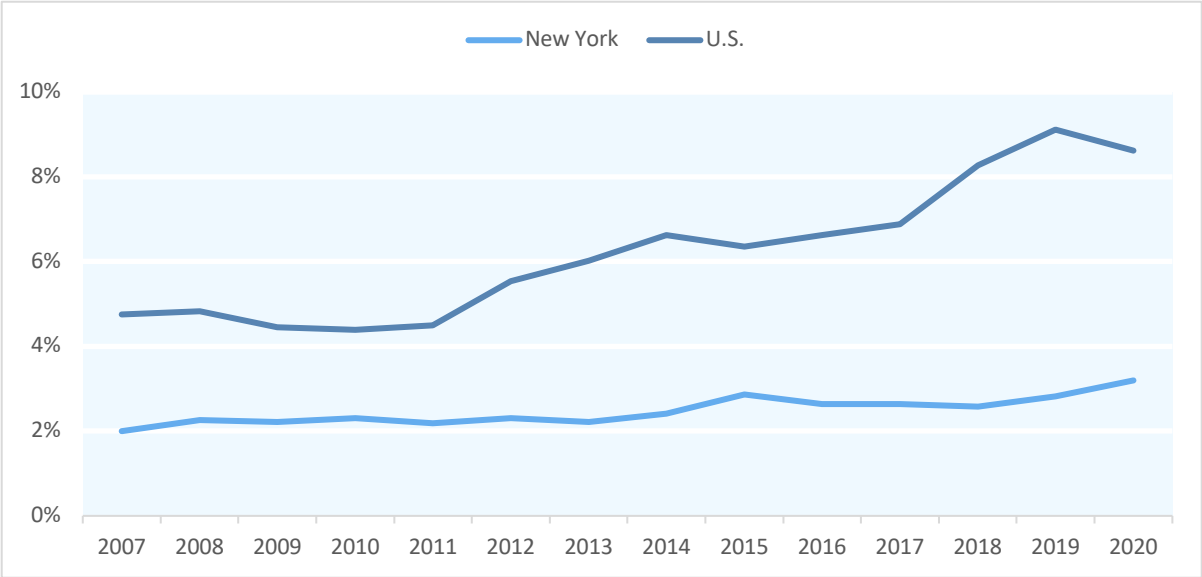
Fiscal Reserves

During sustained economic growth during the 2010s, New York avoided building its fiscal reserve funds

During periods of economic growth states typically reserve a portion of revenue for fiscal reserves. These reserves can be tapped during economic downturns, allowing states to maintain public services and avoid making recession-exacerbating cuts. While New York experienced a period of sustained economic growth during the 2010s, it avoided building its fiscal reserve funds. These funds would have been instrumental during the extreme uncertainty of the Covid recession.

In fiscal year 2007, New York held $1.0 billion in its statutory reserve funds — 2.0 percent of its annual general fund spending. By fiscal year 2020, this level had reached 3.2 percent of spending. Over the same period, reserve levels for all U.S. states had risen from 4.8 percent of spending to 8.6 percent. New York's reserves fell from 10th lowest among U.S. states to 9th lowest.[25]

Figure 10: Fiscal reserves as a percent of general fund spending for New York and U.S. states, fiscal years 2007 to 2020



New York's meager fiscal reserves in 2020 left it among the least prepared states in the country for an economic downturn. While extraordinary federal stimulus largely obviated the need for spending cuts, amid the initial uncertainty of the crisis, the state began to prepare for deep spending cuts that would have drawn out and deepened the pandemic's economic and social toll. Section two of this briefing provides a discussion of the state's fiscal policy during the Covid recession and section five provides an update and outlook for the state's fiscal reserves.

Revenue

Rather than reinvest revenue into public services, the State dispensed revenue gains through tax cuts, with benefits primarily accruing to corporate taxpayers

Spending restraint in the 2010s was a policy choice, not a fiscal necessity. While the Governor restrained spending growth to two percent per year, consistent economic growth in the aftermath of the 2007-09 recession pushed revenue growth above this level. Rather than reinvest this revenue into public services, the State dispensed revenue gains through tax cuts, with benefits primarily accruing to corporate taxpayers and high-income individuals.

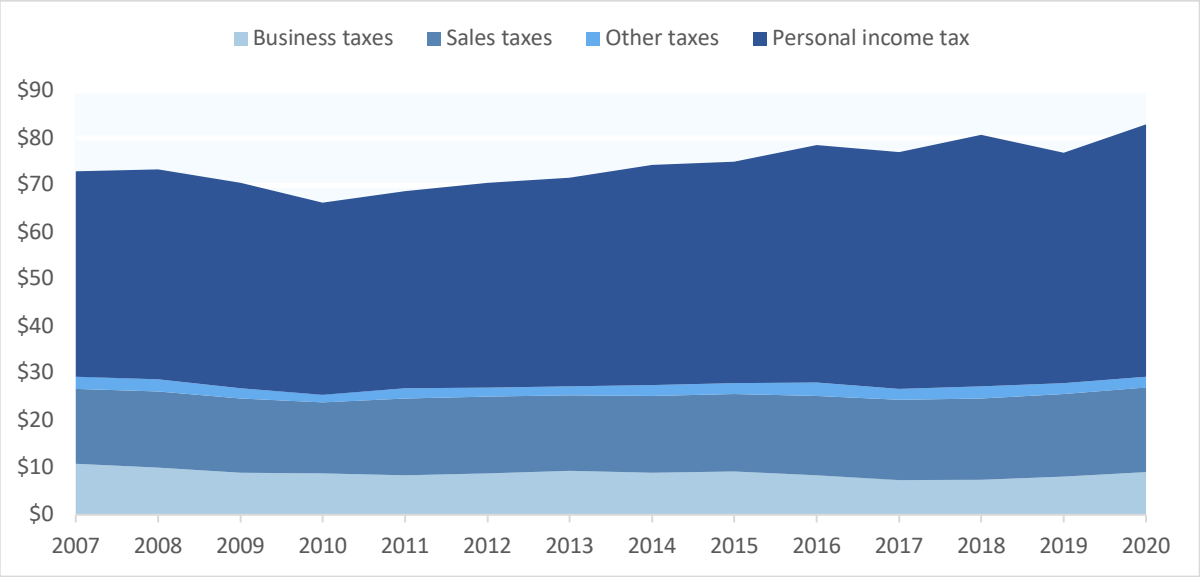
Cuts to the corporate tax and PIT and rising corporate tax breaks had an annual cost of approximately $5 billion. Reductions in PIT rates in 2011 totaled at least $2.6 billion per year.[26] Reforms to the corporate and estate taxes resulted in estimated annual revenue losses of $1.2 billion. Finally, corporate tax breaks hovered around $1.2 billion at their peak, between 2014 and 2018.

New York's tax revenue fell sharply during the recession, from $60.1 billion in fiscal year 2008 to $56.5 billion in fiscal year 2010. Revenue began to rebound the following year. However, revenue growth during the economic recovery was driven almost exclusively by the personal income tax (PIT), the state's largest

tax, comprising 65 percent of tax revenue in fiscal year 2020. Adjusting for inflation, PIT revenue grew by 23 percent between fiscal years 2007 and 2020. This growth accounts for all of the 14 percent overall tax revenue growth over this period. Modest 14 percent growth in sales taxes was fully offset by business taxes, which fell 17 percent, and other taxes, the two largest of which are estate and real estate transfer taxes, which fell 16 percent.

Figure 11: New York tax revenue by source, fiscal year 2007 to 2020

2020 dollars in billions



Because the state's income consistently outpaced revenue collections, New York's effective tax rates fell over this period. In 2007, state tax revenue amounted to 7.0 percent of personal income. By 2019, this ratio had fallen to 6.3 percent. Declining tax rates occurred across all major taxes administered by the state: PIT and corporate effective tax rates fell by 0.3 percentage points, while sales fell by 0.2 percentage points.[27]

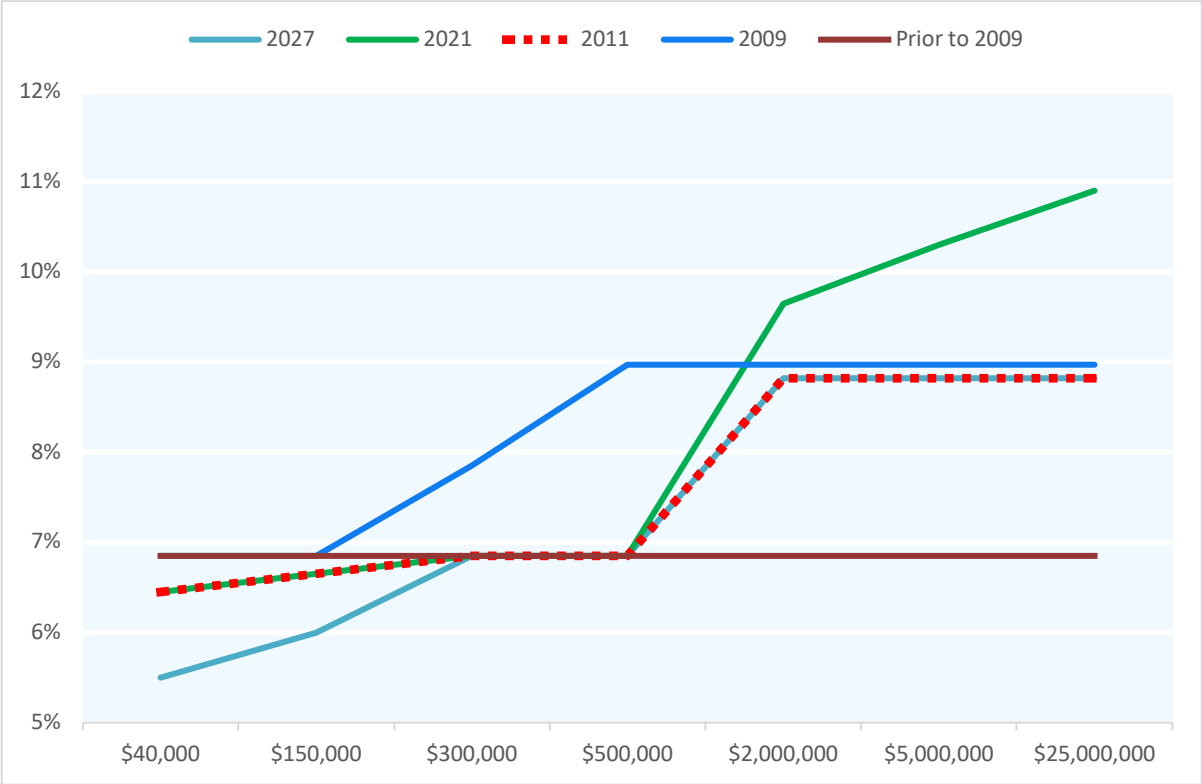
Personal Income Tax

The recovery of PIT revenues in the wake of the financial crisis was attributable, in part, to the creation of new tax brackets on high-income taxpayers. Prior to the crisis, state PIT rates were flat at 6.85 percent for all married, joint filers earning more than $40,000 per year. To fill the budget gap opened by the recession in fiscal year 2009, the State enacted a temporary rate increase on married, joint filers earning more than $300,000 and $500,000. These new brackets were set to expire after three years. Rather than allowing the new brackets to expire altogether, in 2011, the State instead replaced them with a new $2 million bracket, set at 8.82 percent — just below the prior top rate on income above $500,000. These changes set the PIT to drive state revenue growth through the decade and into the current economic recovery.

As New York's fiscal condition continued to improve through the decade, the State in 2016 enacted a "middle class tax cut," lowering rates on income above $40,000, and creating a new, lower bracket on

income above $150,000. The tax cut was originally set to phase in between tax years 2018 and 2025, although the fiscal year 2022 budget accelerated this to take full effect in tax year 2023.

Figure 12: PIT top brackets for tax years following major tax legislation



Notes to chart: rates for married-filing jointly; for years after 2012, brackets shown are rounded down for consistency (actual brackets occasionally adjusted upwards to account for inflation); 2027 reflects full phase in of middle class tax cuts (effective 2023) and expiration of temporary high income surcharge enacted FY22.[28]

Business Taxes

Businesses tax cuts and tax abatements eroded revenue through the 2010s

Businesses tax cuts and tax abatements eroded revenue through the 2010s. Amid recovering revenue in fiscal year 2015, the state enacted sweeping business tax reform lowering liability for corporate taxpayers. The corporate franchise tax (CFT) rate was lowered from 7.1 percent to 6.5 percent — the lowest rate since 1968. Lawmakers also repealed the alternative minimum tax, reduced the base rate at which capital stock base rate, and lowered taxes on manufacturers.[29] These changes, together with a PIT credit tied to a freeze on local property taxes, were expected to cost the state $1.3 billion in fiscal year 2016. The long-run cost is likely far higher, given that changes to the estate tax were phased-in over time. While the Division of Budget did not provide long-run cost estimates, FPI estimated at the time that the business and estate tax cuts alone would cost $1.2 billion annually.[30]

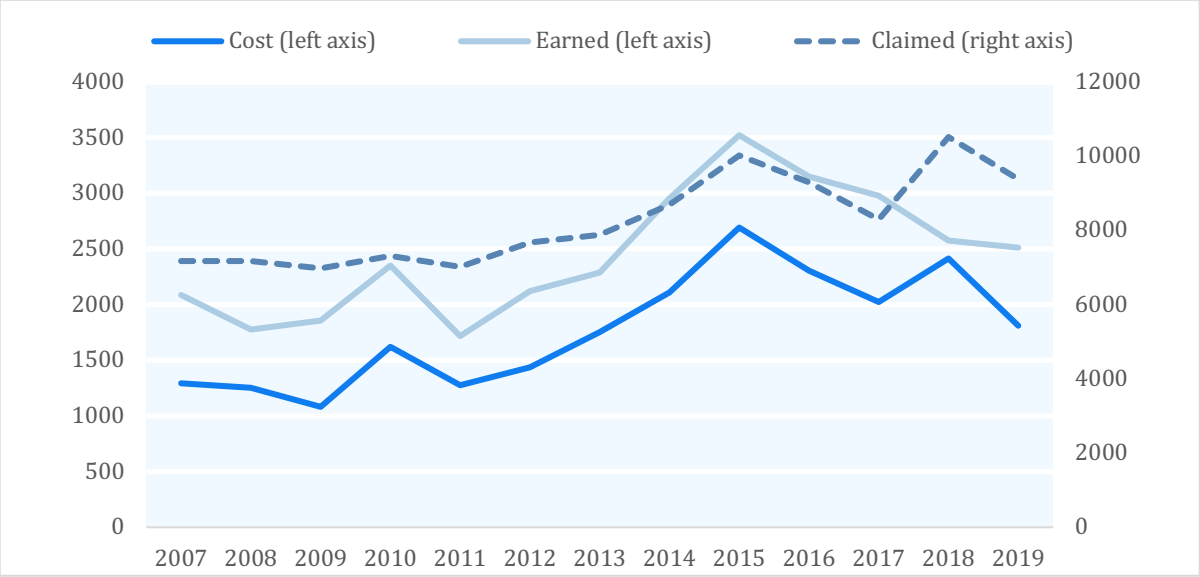
Falling business tax revenue over the 2010s resulted not only from tax rate cuts, but also an expansion of corporate tax credits. In tax year 2019, the most recent data available, corporate tax benefits cost the state

$910 million — 40 percent more than 2007. Corporate tax credit growth was most pronounced between 2011 and 2015, when the cost of benefits more than doubled.

Further, corporate taxpayers earned tax credits worth $1.3 billion in 2019. Corporate tax credits can carry unused tax credits they earned forward into subsequent years. For this reason, earned credits in any given year typically exceed those used. Claimed credits — the accumulation of a given year's earned credits and past years' carried credits — reached $4.7 billion in 2019, 31 percent higher than its level in 2007. Because corporate tax credits can accumulate over time, unrestrained tax credit growth, like that of the mid-2010s, can cost the state for years in the future even if tax credit programs are curtailed.

Figure 13. Corporate tax credit usage, 2007 to 2019

2019 dollars in thousands



Tax incentive growth in the middle of the decade was driven by credits from the Empire Zone program. The program, which granted tax credits for qualified investments in designated economically-marginalized areas, accounted for nearly one-third (32 percent) of all credit used by corporate taxpayers and more than half (54 percent) of credit earned in 2015. This was despite the fact the lawmakers allowed the program to sunset in 2010.[31] Because the program's tax benefit period extends ten years from the start of the investment project, qualified investments continued to accrue tax benefits. In 2019, the program still cost $103 million.

As evidence of Empire Zone's weak performance incentivizing new investment, lawmakers replaced that program with the Excelsior Jobs Program.[32] The reworked program, the flagship economic development program administered by the Empire State Development Corporation, continues to include provisions targeting economically-distressed areas. However, Excelsior primarily targets select industry groups, regardless of location. Initially focused on manufacturing, industry targets have been expanded to provide greater benefits to green projects and child care services. As of 2019, Excelsior costs have remained low, with current year costs, earned credits and claimed credits all holding at $20 million. Nevertheless, the costs of the Empire Zone Programs are instructive. Excelsior's benefit period, which allows most program participants to claim credits over a ten year period, may similarly allow costs to accumulate, even if program

changes are made.[33] More recent data from the Tax Expenditure Report suggests the program's costs may be rising quickly, to an estimated $120 million in 2020.[34]

In 2019, the costliest corporate tax credit, and the leading source of growth in recent years, was the Film Production Tax Credit. The credit allows film producers to claim a tax benefit against film production expenses. Lawmakers expanded the program considerably in 2009, from annual allocation of $25 to $420 million. If annual allocation is fully subscribed, production companies can draw subsequent years' allocations, creating a tax benefit overhang.[35]

The state's second costliest credit in 2019 were the Brownfield Tax Credits, a suite of three programs providing credits for costs related to remediation of industrial sites. The program with the second most claimed credits, after Empire Zones, was the Investment Tax Credit, which provides tax abatements–refundable for new businesses–for capital investments.[36]

Figure 14. 2019 top corporate tax credits

	Cost	Earned	Claimed
Empire State Film Production Credit	$401	$476	$406
Brownfield Tax Credits	$140	$140	$140
Empire Zone Credits	$103	$245	$2,353
Investment Tax Credit	$65	$223	$1,550
Low-Income Housing Credit	$53	-	$54
Historic Properties Rehabilitation Credit	$45	$43	$47
Special Additional Mortgage Recording Tax Credit	$26	$26	$63
New York Youth Jobs Program Tax Credit	$25	$25	$25
Excelsior Jobs Program Credit	$20	$20	$20

Source: New York State Department of Taxation and Finance.[37] Investment Tax Credit includes the smaller Investment Tax Credit for the Financial Services Industry and Empire State Film Production Credit includes smaller Empire State Film Post Production Credit.

Other Tax Policy Changes

Estate

The fiscal year 2015 tax reform made changes to the state's tax system beyond business taxes. The costliest permanent change was recoupling the state's estate tax to the federal policy. Previously, the state's estate tax exempted estate holdings below $1 million. Estate holdings above this exclusion threshold are subject to estate tax. In conforming with federal policy, the exclusion was raised substantially and indexed to inflation. As of tax year 2023, the state estate tax exclusion is $6.58 million.[38]

Sales

Sales taxes were not subject to significant change over the 2010s, and were steadily buoyed by economic growth. The state sales tax and metropolitan commuter transportation district remained at four percent and three-eighths of one percent, respectively, since 2005. Given limited revenue options from the state, several local governments facing fiscal shortfalls in 2009, including New York City, raised sales tax rates. As local government financing remained strained in the face of state-imposed property tax caps, several other counties, Westchester and Ulster, raised their sales tax rates in 2014 and 2019. Higher county rates must be approved by state lawmakers. For many counties, these rates are set to expire November 30, 2023.[39]

Yachts & Jets

New York State continued to add to the wide array of exemptions to its sales tax. In 2015, sales tax was exempted on vessels costing more than $230,000. Aircraft and machinery and equipment for general aviation aircraft (commercial aircraft were already exempt) were also exempted. This added to existing, and costly, tax breaks for the aviation industry, including exemptions for food and fuel sold to airlines.[40]

Public Workforce

A decade of state fiscal retrenchment battered the public workforce

A decade of state fiscal retrenchment battered the public workforce. Between 2007 and 2019, the number of New York State employees fell by 6,750 — a 2.9 percent decrease. Losses were concentrated in the years after the 2007-09 recession, with the state workforce falling continuously between 2008 and 2012. While public employment began to recover, it stabilized in 2017 at a level below its pre-recession levels. State employment's share of all jobs fell from 2.8 percent to 2.4 percent by 2019. The Covid recession pushed state employment to new lows, falling 12,800, or 5.6 percent, between 2019 and 2021.

Figure 15. New York State employment, 2001-2021

Public employment losses following the 2007-09 recession were led by declining employment at the state's public hospitals, which fell by 1,600, or 8 percent. Employment at state-supported educational institutions, including the State University of New York, rose during this period, while all other state employment fell by 7 percent.

Figure 16. State employment change, 2007 to 2019 and 2019 to 2021 by function

	Change 2007-19	Change 2019-21
Education	14%	0%
Hospitals	-8%	-2%
All other	-7%	-6%

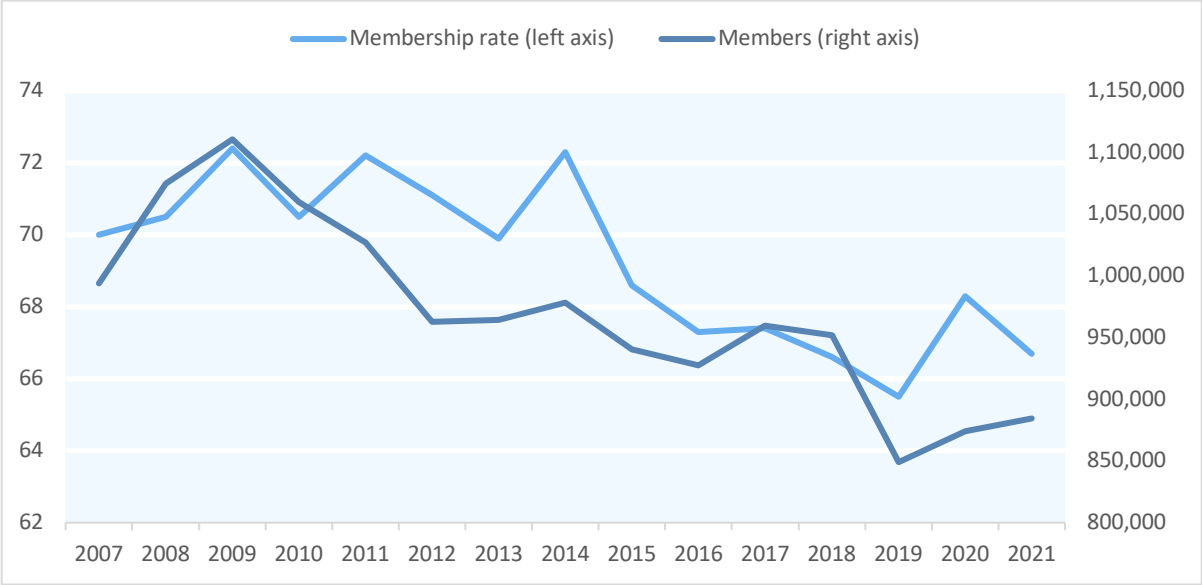
New York City saw the steepest decline in its state workforce. The city's losses between 2007 and 2019 accounted for 88 percent of the state's net losses. Beyond the city, losses in other regions, including the Hudson Valley and Southern Tier, were offset by gains in Long Island and Central New York. During the recession, state employment losses were more consistent across the state.

Figure 17. State employment change by region, 2007 to 2019 and 2019 to 2021

Region	2007	2019	2021	Change 2007-19	Change 2019-21
Capital District	53,430	52,156	49,235	-2.4%	-5.6%
New York City	41,403	35,460	33,454	-14.4%	-5.7%
Hudson Valley	26,826	24,332	22,749	-9.3%	-6.5%
Western New York	23,916	24,094	22,343	0.7%	-7.3%
Long Island	21,342	23,926	23,444	12.1%	-2.0%
Central New York	15,174	18,756	18,159	23.6%	-3.2%
Finger Lakes	14,568	14,346	13,207	-1.5%	-7.9%
North Country	12,951	13,350	12,134	3.1%	-9.1%
Southern Tier	12,151	11,261	10,618	-7.3%	-5.7%
Mohawk Valley	10,983	10,325	9,869	-6.0%	-4.4%
Statewide	234,947	228,195	215,398	-2.9%	-5.6%

Eroding state employment took a toll on New York's labor unions. Between 2007 and 2019, membership in unions representing New York's public workforce fell 15 percent. The share of the public workforce who were members of unions fell from 70 percent to 66 percent over the same period.[41]

Figure 18. New York public union membership and membership rate, 2007 to 2021



Social and Economic Results of Fiscal Stagnation

The 2010s were a lost fiscal decade for New York, characterized by declining social investment and tax cuts and rising tax breaks for corporate taxpayers. In the wake of this fiscal retrenchment, the economic polarization that already characterized the state's economy accelerated. Struggling regions of Upstate New York lost population and jobs. Almost all economic growth was generated by New York City. The city's growth model, marked by the dual growth of high-wage and low-wage jobs and a declining middle, cemented the state's place as the highest inequality state in the U.S.

Population Growth

New York State's population grew 4.2 percent, to 20.2 million, between 2010 and 2020. The state appears to have experienced a faster pace of growth in the first half of the decade.[42] Following 2016, slowing international immigration and accelerating domestic outmigration slowed the pace of the state's population growth. The state's population growth concentrated in New York City and its surrounding regions, the Hudson Valley and Long Island. Taken together, growth in these three downstate regions accounted for 84 percent of the state's population. Four Upstate New York regions experienced population loss over the 2010s. Section two of this briefing provides a detailed analysis of recent New York State population trends.

Figure 19. Population growth by region, 2010 to 2020

Region	2010	2020	Percent change
New York State	19,378,117	20,201,249	4.2%
New York City	8,174,930	8,804,190	7.7%

Hudson Valley	2,290,993	2,398,150	4.7%
Long Island	2,832,970	2,921,694	3.1%
Capital District	1,079,217	1,106,088	2.5%
Western New York	1,399,775	1,418,057	1.3%
Finger Lakes	1,217,046	1,222,868	0.5%
Central New York	791,943	785,114	-0.9%
Southern Tier	657,942	640,036	-2.7%
North Country	433,203	421,694	-2.7%
Mohawk Valley	500,098	483,358	-3.3%

Regional Economics

Regional economic trends in New York in the 2010s followed the same pattern as population growth. The 813,000 jobs created in New York City between 2008 and 2019 comprised 87 percent of all jobs created in New York State. New York City's neighboring regions also added jobs, while the same four Upstate New York regions that lost population also lost jobs.

Figure 20. Employment growth by New York State region, 2008 to 2019

Region	2008	2019	Percent change
New York State	8,608,351	9,542,899	11%
New York City	3,679,345	4,492,732	22%
Long Island	1,225,878	1,298,023	6%
Hudson Valley	895,670	940,849	5%
Capital District	510,136	529,202	4%
Finger Lakes	548,795	561,491	2%
Western New York	631,462	634,844	1%
Central New York	350,436	347,054	-1%
North Country	155,866	151,573	-3%
Mohawk Valley	197,387	191,434	-3%
Southern Tier	275,593	257,691	-6%

New York City's already dominant position in the state economy continued to expand. Between 2008 and 2019, the city was responsible for 82 percent of the entire state's GDP growth. Its share of the state's total GDP rose 6.4 percentage points while its share of jobs rose 4.3 percentage points, despite population gains of just 1.4 percentage points.

Figure 21. New York City share of State by selected indicators

	2008	2020
GDP	52.4%	58.6%
Employment	42.7%	47.1%
Total Wages	56.9%	59.7%
Population	42.2%	43.6%

The dynamics underlying New York State's wage growth brings the state's high-inequality economic model into sharper relief. As with population and job growth, total wages — the aggregate wage bill for all employees — grew the most quickly in New York City, rising 23 percent, after adjusting for inflation. However, the city's average wage grew just one percent, after adjusting for inflation. This growth was far lower than that of any other region. New York City's high total wage growth, but low average wage growth, provides important insight into the unbalanced pattern of growth driving New York's economic expansion.

Figure 22. Total and average wages by region, 2008 to 2019

2019 dollars

	Total wages (billions of dollars)			Average wages		
	2008	2019	%	2008	2019	%
New York State	$ 612	$ 719	17%	$ 71,125	$ 75,365	6%
New York City	$ 348	$ 430	23%	$ 94,687	$ 95,626	1%
Capital District	$ 26	$ 29	15%	$ 50,081	$ 55,592	11%
Long Island	$ 73	$ 81	12%	$ 59,237	$ 62,692	6%
Western New York	$ 28	$ 31	11%	$ 44,842	$ 49,484	10%
Central New York	$ 16	$ 18	8%	$ 46,851	$ 51,001	9%
Hudson Valley	$ 55	$ 59	8%	$ 61,177	$ 62,747	3%
Finger Lakes	$ 26	$ 28	8%	$ 48,169	$ 50,684	5%
North Country	$ 6	$ 7	6%	$ 41,332	$ 44,989	9%
Mohawk Valley	$ 8	$ 8	5%	$ 40,544	$ 43,982	8%
Southern Tier	$ 13	$ 13	2%	$ 46,375	$ 50,835	10%

Counterintuitively, average wages grew, after adjusting for inflation, in every borough in New York City. However, average wages are highly unequal across the city. The average wage of jobs based in Manhattan was $127,500 in 2019, more than twice that of any other borough. While wages rose in every borough, employment growth was also uneven across the city. Jobs grew more quickly in the outer boroughs than in Manhattan. This changing composition in the geography of jobs pulled down the average wage for the city as a whole. This disproportionate creation of lower-wage jobs and persistent wage gaps between the professional and services sectors is a central feature of New York's model of economic growth.

Figure 23. Average wage and employment growth by New York City borough, 2008 to 2019

	Average wages			Employment		
	2008	2019	%	2008	2019	%
Bronx	$ 51,620	$ 58,396	13%	226,301	324,446	43%
Kings	$ 46,257	$ 50,585	9%	479,248	795,104	66%
New York	$119,254	$127,525	7%	2,376,385	2,527,343	6%
Queens	$ 52,963	$ 57,449	8%	503,780	717,786	42%
Richmond	$ 47,632	$ 54,045	13%	93,631	128,053	37%

New York State's economic growth in the 2010s was driven by the dual expansion of high-paying professional services jobs and low-pay service sector jobs in New York City. This divergence of the labor market into high- and low-paying jobs and declining middle-wage jobs accelerated in the aftermath of the 2007-09 recession, but had roots extending decades in the past. According to labor economist David Autor, the U.S. labor market has been characterized by rising wages for highly educated workers, falling wages for less educated workers, and fewer jobs in the middle of income distribution since 1980.[43] However, the extent of this divergence, or labor market polarization, has been uneven across the U.S.

Labor market polarization is driven by the twin phenomena of deindustrialization and the shift in economic production toward high-wage, knowledge-intensive sectors of the economy. In turn these high value-add sectors have tended to generate demand for new service sectors, generally staffed by less-education, low-wage workers. In recent decades, metropolitan areas with high population density have experienced greater polarization than the rest of the U.S. Dense metropolitan areas tend to have high concentrations of college educated workers, and are conducive to the development of emerging high-wage industrial clusters, including in the financial services and information technology sectors. As the number of high-education professional jobs has increased in dense cities, middle-wage production and administrative jobs have fallen.

These formerly middle wage jobs have increasingly been replaced by low-wage, low-education service sector jobs.

New York State's economic geography left it highly exposed to labor market polarization. The New York metropolitan area's density and concentrations of college-educated workers primed the region for the fast development of both high- and low-wage economic sectors. Meanwhile, the formerly production-intensive regions of Upstate New York have tended to falter, without the counterbalance of emerging industrial sectors.

Figure 24. Share of population 25 and over with a bachelor's or higher

New York State	37%
Long Island	42%
Hudson Valley	41%
New York City	39%
Capital District	37%
Finger Lakes	34%
Western New York	31%
Central New York	31%
Southern Tier	29%
Mohawk Valley	25%
North Country	23%

These dynamics have also primed New York for nation-leading economic inequality. In the 1980s, as labor market polarization began to become more pronounced, income inequality in New York began to rise. While the state had been no more unequal than the rest of the U.S., by 2015, the state was home to the highest inequality in the country. This inequality was the direct result of increasing wealth — and concomitant rise in low-wage work — in the New York metropolitan area.[44] Recent data suggests the Covid recession has likely continued this trend, as Downstate New York rebounds and struggling regions of Upstate New York remain stagnant.

Fiscal Policy During the Covid Recession

The social and economic costs of Covid hit New York State earlier and harder than the rest of the country. The U.S.'s first major epicenter, New York suffered devastating loss of life in the first months of the pandemic. The health crisis took a severe economic toll. Between February 2020 and April 2020, the state lost nearly two million jobs, a 20.2 percent drop. For the U.S. overall, 14.4 percent of jobs were lost in the Covid recession. The number of active claims for unemployment insurance in the state rose from 167 thousand immediately before the March lockdowns to 2.2 million in May 2020. New York's unemployment rate reached a peak of 16.5 percent in May 2020, nearly two percentage points higher than the U.S. rate.

The suddenness and severity of the social need and economic dislocation created by the crisis caused enormous uncertainty for the state's fiscal health. This hampered the state's ability to mount a meaningful policy response. New York's fiscal year 2021 budget passed April 2, 2020, only a few weeks after the first lockdown orders took effect. The enacted budget financial plan was drafted on the assumption that the budget would become unbalanced as the Covid recession deepened and revenues plunged. To restore balance, the budget included provisions to allow the Director of Budget to reduce spending as necessary, with revenue and spending levels undergoing continual reassessment throughout the fiscal year.

Extraordinary federal stimulus largely obviated the need for such cuts. The fiscal year 2021 executive budget proposal, released in January 2020, expected state operating funds spending to reach $105.8 billion. The enacted budget financial plan lowered planned state spending to $94.5 billion, with cuts to aid-to-localities to be determined over the course of the fiscal year. Responding to economic conditions, this figure was lowered in the fiscal year's first quarter and subsequently slightly raised in the mid-year update. In the end, actual state spending totaled $104.2 billion in fiscal year 2021. This was largely the result of federal relief funding. Direct federal emergency relief drove actual funds spending, which includes state and federal revenue, higher than the level projected in the enacted budget, from $177.8 billion to $186.6 billion. At the same time, that even the state's own-source spending largely avoided cuts is a testament to the unprecedented level of federal stimulus.

Federal stimulus and emergency relief was enacted in a series of federal legislation beginning March 2020 and culminating in the March 2021 American Rescue Plan (ARP) Act. Funding appropriated by this federal legislation lifted state receipts through several channels. Most straightforwardly, direct aid to states and

localities provided flexibility for local governments to replace revenue losses and expenses related to the pandemic. The March 2020 Coronavirus Aid, Relief, and Economic Security (CARES) Act allocated $5.1 billion to New York, while the ARP allocated $12.7 billion.[45]

Federal legislation provided further direct fiscal relief by increasing the federal medical assistance percentage (FMAP, the share of Medicaid costs paid by the federal government) by 6.2 percentage points. In fiscal year 2021, this FMAP enhancement lowered state Medicaid costs by $3.4 billion, or 13 percent of state Medicaid costs.[46] Further direct fiscal support was provided through education aid, including support for school districts as well as SUNY and CUNY, rental assistance, and a host of other federal funding streams tied to specific spending programs. These programmatic federal appropriations drove the state's Covid response policy, especially in the first year of the pandemic.

Finally, federal stimulus directly to households and businesses bolstered the state's fiscal condition. The CARES Act included an unprecedented expansion to unemployment insurance (UI), adding $600 per week to existing UI benefits, lengthening the period recipients can draw benefits, and creating a program to allow self-employed workers to claim UI. Three pieces of legislation — CARES, the Consolidated Appropriations Act of 2021, enacted December 2020, and the ARP — provided one-off stimulus payments totaling $2,600 to low- and middle-income households. A suite of tax credits, loans, and grants to businesses, foremost of which was the Paycheck Protection Program, afforded a lifeline to firms affected by the pandemic. This extraordinary stimulus increased household income, stabilized consumer spending, and accelerated the economic recovery, raising state tax revenue above initial estimates.

For the first year of the crisis, fiscal year 2021, New York fiscal policy was largely reactive and dependent on federal stimulus as a fiscal and economic lifeline. Revenue was buoyed by federal legislation and spending was generally set by federal crisis response priorities. For fiscal year 2022, this dynamic changed. New York State lawmakers set their own policy priorities to support the economic recovery alongside ongoing federal relief programs. These state-funded programs included $200 million for rental and homeowner assistance, an $865 million suite of grants for small businesses, and the $2.1 billion excluded workers fund, which sent payments designed to mirror enhanced UI benefits to workers who were unable to access those programs, mainly as a result of immigration status. The fiscal year 2021 budget also boosted school aid by by $3.0 billion, more than restoring prior-year cuts.

To finance these new programs and funding restorations, New York State raised taxes in fiscal year 2022 for the first time since the 2008 financial crisis. Lawmakers raised personal income tax (PIT) rates on income above $2 million and created two new brackets for those earning more than $5 million and $25 million per year.[47] These new rates were projected to raise $2.8 billion in fiscal year 2022, rising to $4.5 billion in fiscal year 2025. They are set to expire in tax year 2027.

New York lawmakers also raised the state's corporate franchise tax (CFT). For corporate taxpayers with business income of more than $5 million, CFT rates rose from 6.5 percent to 7.25 percent. Both the PIT and CFT rate increases took effect in tax year 2021, although PIT high-income brackets remain in effect through tax year 2027, while CFT rates were set to expire after tax year 2023.[48]

Figure 25. Fiscal year 2022 revenue estimates for new PIT and CFT rate

Dollars in millions

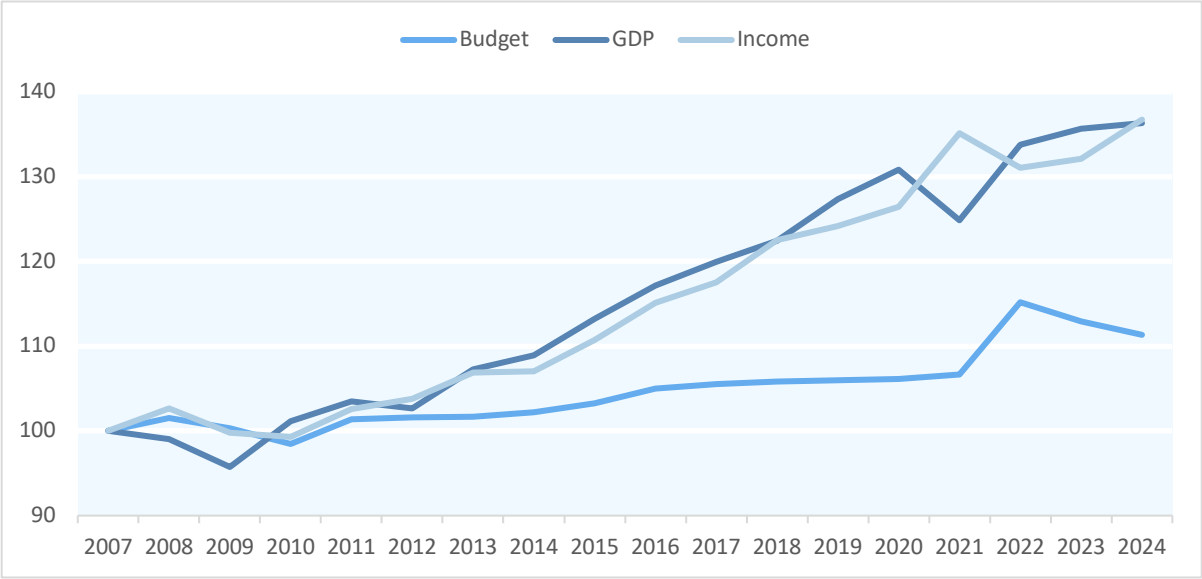
	FY22	FY23	FY24	FY25
PIT	$2,753	$3,251	$3,439	$4,472
CFT	$750	$1,073	$796	–

Post-Covid Fiscal Policy: a Return to Status Quo

The federal and state policy responses led to a surge in funding for pandemic relief, social assistance, and economic recovery programs. The resulting economy was far faster than the one following the 2008-09 recession. The unprecedented level of federal relief led income to rise even as GDP fell in the first year of the crisis. The state's GDP caught up the following year, as income level-set amid expiring federal aid. By fiscal year 2024, New York's personal income and GDP are expected to exceed fiscal year 2020 levels by 8.2 percent and 4.2 percent, respectively, after adjusting for inflation. New York's economic growth and revenue actions allowed the state budget to keep pace with income to an extent not seen since before the 2008-09 recession.

Figure 26. State operating funds spending, GDP, and personal income, fiscal years 2007 to 2024

Indexed to 2007 (adjusted for inflation)



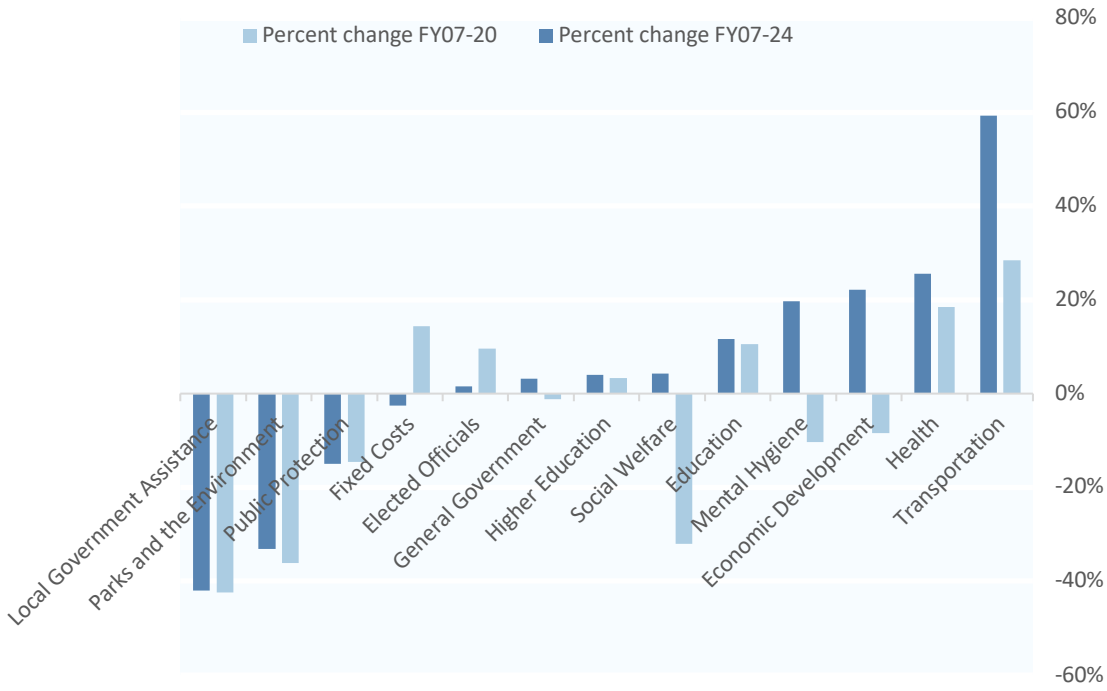
New state operating spending restored funding for some programs eroded in the decade following the 2008-09 recession, and pushed other areas to new highs. Funding for social welfare is set to expand the most of any program area. Having fallen 32.0 percent between fiscal years 2007 and 2020, after adjusting for inflation, social welfare state spending would rise 53.3 percent between fiscal years 2020 and 2024, under the executive budget. Growth is attributable to mechanical increases in spending as public assistance caseloads rise amid economic turmoil, temporary relief programs administered by OTDA, including rental assistance and support for asylum seekers, and new recurring spending related to childcare. This recent, and largely temporary, growth in social welfare would bring fiscal year 2024 spending 4.2 percent above fiscal year 2007 inflation-adjusted levels.

Recent spending growth has also raised health, mental hygiene, and transportation funding. The former two programmatic areas are comprised of the core agencies responsible for responding to Covid and have continued to support elevated Medicaid caseloads. Higher transportation spending is also a direct response to Covid. The pandemic caused seemingly lasting structural change in the MTA's budget, as ridership remains persistently below pre-Covid levels, depressing fare revenue. In response, the state has proposed increasing recurring state and city operating support for the transit system.

Other programmatic areas have not significantly changed in the wake of Covid. Higher education and local government assistance have seen little funding change, after adjusting for inflation. As a result, proposed higher education spending in fiscal year 2024 remains nearly flat from fiscal year 2007 levels. Local government assistance remains about 42 percent lower over the same period.

Figure 27. State spending change by programmatic area, fiscal years 2007 to 2020 and 2024

Adjusted for inflation



The fiscal year 2024 executive budget would raise state operating funds spending by 2.0 percent. Given high recent inflation, this spending would represent a decrease of 1.4 percent, after adjusting for inflation. Inflation adjusted state spending also fell in fiscal year 2023. Recent spending growth was concentrated in just one year–fiscal year 2022–when strong economic growth and new revenue buoyed state spending. After rising temporarily after fiscal year 2022, the state budget's share of GDP is set to return to 5.7 percent—the same level as fiscal year 2020. Fiscal year 2024 spending growth would be just 11 percent above fiscal year 2007, after adjusting for inflation. Over the same period, the state's GDP and personal income grew 36 percent and 37 percent, respectively.

These trends raise the question of whether New York's Covid-era fiscal policy represents an aberration or new approach. The revenue actions and social assistance enacted in fiscal year 2022 represented a distinct break with fiscal policy making in the aftermath of the last recession the ensuing decade. Many of the enacted changes on both the revenue and expenditure side, however, were temporary. As economic uncertainty looms in the year ahead, the state will face the same decisions as the last two crises: extend and expand programs to tackle these challenges as they arise or cut and restrain New York's public services.

Appendix

State spending change by programmatic area, fiscal years 2007 to 2020 and 2024

Fiscal year 2024 dollars in millions

Programmatic area	2007	2020	2024	Change, 2007-20	Change, 2007-24
Economic Development and Government Oversight	$904,030	$827,907	$ 1,103,789	-8.4%	22.1%
Education	$33,923,131	$37,495,503	$37,890,389	10.5%	11.7%
Elected Officials	$4,000,426	$4,384,829	$4,060,449	9.6%	1.5%
Fixed Costs	$11,853,144	$13,560,000	$11,548,155	14.4%	-2.6%
General Government	$1,856,591	$1,834,061	$1,914,588	-1.2%	3.1%
Health	$24,495,189	$29,002,369	$30,742,464	18.4%	25.5%
Higher Education	$10,472,919	$10,825,675	$10,884,997	3.4%	3.9%
Local Government Assistance	$1,449,702	$834,482	$841,776	-42.4%	-41.9%
Mental Hygiene	$8,224,521	$7,372,404	$9,844,736	-10.4%	19.7%

Parks and the Environment	$814,963	$521,142	$545,415	-36.1%	-33.1%
Public Protection/ Criminal Justice	$5,675,002	$4,850,996	$4,825,893	-14.5%	-15.0%
Reclassification/ Miscellaneous	$323,609	$ (79,353)	$190,611	-124.5%	-41.1%
Social Welfare	$4,908,380	$3,336,937	$5,115,136	-32.0%	4.2%
Transportation	$3,565,484	$4,577,323	$5,676,339	28.4%	59.2%
TOTAL	$ 112,467,091	$119,344,275	$ 125,184,737	6.1%	11.3%

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