

# OPTIONS FOR ACHIEVING ADEQUACY

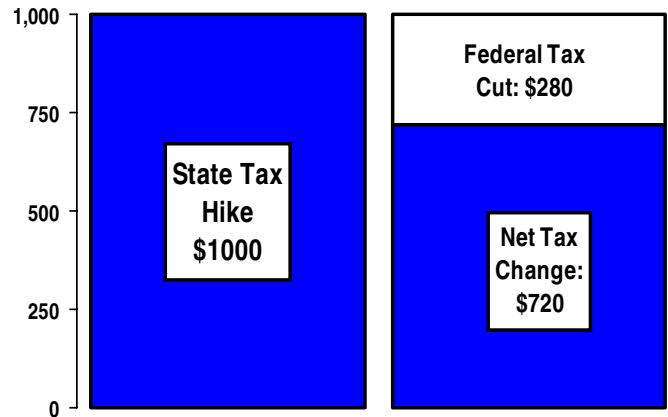
As New York lawmakers struggle to raise revenue for education and other public services, they face an important choice between three tax strategies: **broadening the base** of New York taxes to include currently exempt items (for example, by expanding the income tax to include all pension income, including more services in the sales tax base, or eliminating corporate income tax loopholes), **increasing the rates** of these taxes, or looking to entirely **new revenue sources** that the state does not currently use. Base-broadening is the best place to start in achieving structural tax reform—but loophole-closing will be insufficient to meet the state's revenue raising needs, so lawmakers may also be forced to increase tax rates or introduce new taxes. This chapter describes various options that could help to resolve New York's fiscal shortfall.

Most of the proposals described here would increase New York taxes, but the chapter also includes several revenue-reducing options that could be adopted in conjunction with revenue-raising reforms to mitigate the impact on low- and middle-income taxpayers. **In each case, this chapter estimates the annual revenue impact of the proposals if enacted in calendar year 2006.**

For each option described in this chapter, the accompanying bar charts show the impact of these options on each New York income group, expressed as a share of that group's income. The solid portion of each bar represents the net tax change (after taking federal tax changes into account) for each income group. The transparent portion of each bar shows the amount of state tax change that is offset immediately by federal tax changes. For New Yorkers who itemize deductions on their federal tax returns, changes in state income and property taxes can produce offsetting changes in federal tax liability. When state and federal taxes interact in this way, it is important to assess the effect of state tax proposals on the *overall* taxes paid by New Yorkers, including federal state taxes, as the following example shows.

Suppose an itemizing New York taxpayer in the 28 percent federal tax bracket is subject to a \$1,000 increase in New York income taxes. The value of his or her federal itemized deductions will increase by \$1,000. This means that \$1,000 *less* of this taxpayer's income will be subject to federal tax after the New York tax cut. Since this last increment of

**How Increases in Federally Deductible Taxes Reduce Federal Tax Burdens:  
An Example**



income is taxed at 28 percent, this person's federal tax liability decreases by \$280. So the *total* tax hike for this itemizing New York taxpayer from a \$1,000 increase in state tax liability is actually \$720, not \$1,000. Our distributional analysis of this proposal (the second column in the chart above) shows that taxpayers do not pay the full \$1,000 tax hike, since \$280 of that hike is directly offset by federal tax cuts. An analysis that looked only at the *state* tax impact of the proposal (the first column in the chart) would overstate the tax increase on New Yorkers.

State and local property taxes are also deductible on federal tax returns, so a similar percentage of property tax increases on New York taxpayers who itemize will be offset by federal tax cuts.

If, on the other hand, the same itemizing New York taxpayer was subject to a \$1,000 sales tax hike, federal taxes would not change, because sales taxes generally cannot be deducted.<sup>25</sup> This means that the whole \$1,000 tax hike would be paid by the taxpayer. In this example, the choice between sales and income taxes does not affect state revenues—the state receives an extra \$1,000 with either approach—but the New York taxpayer fares much worse under the sales tax than under the income tax.

<sup>25</sup>Due to a temporary tax break enacted by Congress in 2004, federal itemizers can choose between writing off sales taxes and income taxes in 2004 and 2005—but for almost all New York residents, deducting income taxes will always be a better option.

This “federal offset” is most important to wealthier taxpayers, who are more likely to itemize federal returns and pay at higher marginal rates. Low-income New Yorkers, who tend not to itemize their federal returns, are unaffected by this federal interaction.

## Building Blocks for Tax Reform

This section shows the impact of a variety of tax changes that could be implemented to raise (or reduce) New York tax revenues. Since none of these options are individually sufficient to meet the state’s spending needs, the following section combines these “building blocks” into larger packages of revenue-raising plans that could raise the \$8.5 billion that may be needed to adequately fund services.

### A. State Personal Income Tax Rate Changes

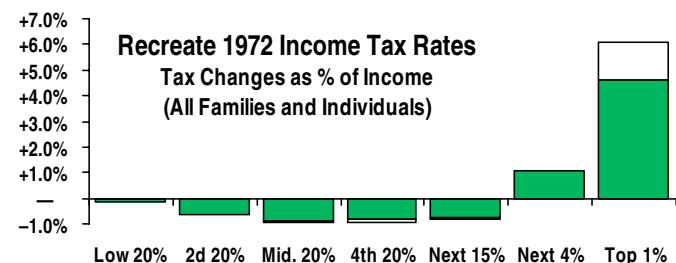
#### 1. Recreate 1972 Income Tax Rates

##### Principal Features

- Increases New York taxes by \$6.7 billion.
- Decreases federal taxes by \$2 billion.
- Tax cut for 95 percent of taxpayers, on average.

##### Discussion

New York’s state income tax brackets and rates are less progressive than they have been in the past. This option undoes the income tax rate cuts enacted over the past thirty years, reimposing the tax rate structure as it existed in 1972. The 1972 income tax rates ranged from 2 percent to 15 percent. The 1972 tax brackets are indexed for inflation, so the 15 percent top marginal rate would apply to taxable income over \$236,000 in 2006. This option would raise \$6.7 billion in New York tax revenues, of which \$2 billion, or 29 percent of the state tax hike, would be offset by lower federal income tax payments for New York itemizers.



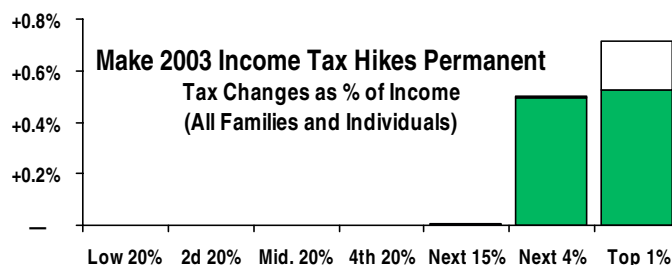
#### 2. Make 2003 Temporary Income Tax Rate Hikes Permanent

##### Principal Features

- Increases New York taxes by \$1.5 billion.
- Decreases federal taxes by \$285 million.

##### Discussion

In 2003, New York lawmakers enacted a temporary income tax surtax on the wealthiest taxpayers, with new top tax rates of 7.5 percent (on taxable income above \$150,000 for married couples and \$100,000 for single taxpayers) and 7.7 percent (above \$500,000 of taxable income for all families) for tax year 2003. The higher tax rates are currently scheduled to gradually decrease in 2004 and 2005, and will sunset at the end of 2005. This option would make the top rates—as they were imposed in 2003, with a top rate of 7.7 percent—a permanent part of the state income tax. Nineteen percent of the state tax hike from this option would be offset by lower federal income taxes for New York itemizers.



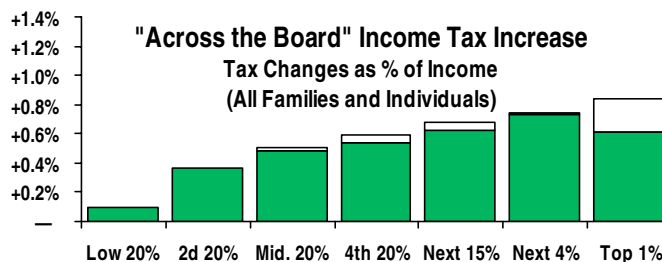
#### 3. “Across the Board” Income Tax Increase

##### Principal Features

- Increases New York taxes by \$4.2 billion.
- Decreases federal taxes by \$500 million.

##### Discussion

This option increases the importance of the personal income tax in New York’s tax system, but does not make the tax more progressive. The option



would increase all of the income tax rates by 10 percent, resulting in a tax hike for those currently paying state income taxes. Because the poorest New Yorkers generally pay no income tax, this option would not impact low-income New Yorkers substantially. 12 percent of the state tax hike from this option would be offset by lower federal taxes for itemizers.

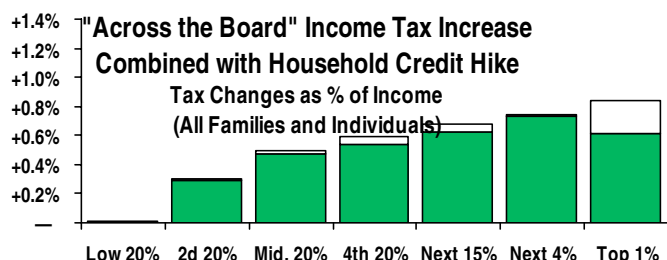
#### 4. “Across the Board” Income Tax Increase Combined with Household Credit Hike

##### Principal Features

- Increases all New York income tax rates.
- Increases the household credit by \$50.
- Increases New York taxes by \$4.15 billion.
- Reduces federal taxes by \$500 million.

##### Discussion

This option is more progressive than the “across the board” income tax hike in option 3 because part of the tax hikes on low-income taxpayers are offset by an expansion of the household credit. This change combines a 10 percent income tax hike with a \$50 increase in the maximum household credit (for all those currently eligible for the credit). 12 percent of this state tax hike would be paid for directly by the federal government in the form of federal income tax cuts for New York itemizers.



#### 5. Tax Unearned Income at a Higher Rate

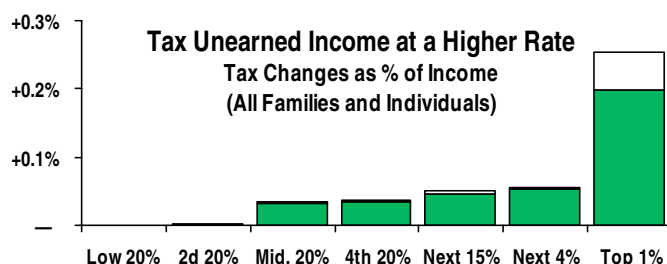
##### Principal Features

- Applies a higher tax rate to unearned income such as capital gains and dividends.
- Increases New York taxes by \$600 million.
- Reduces federal taxes paid by \$98 million.

##### Discussion

Until 1988, New York taxed earned and unearned income under separate rate schedule, with a lower top rate on earned income (12 percent) than on unearned income such as capital gains and dividends (14 percent). This option re-imposes a higher income

tax rate schedule on capital gains and dividends. These income sources are taxed at a rate 1 percentage point higher than other income sources, so income that would be taxed at 6.85 percent under the regular income tax would instead be taxed at 7.85 percent under this option. Because wealthier New Yorkers receive most dividends and capital gains, this is a very progressive tax increase. A substantial portion of this tax hike never comes out of the pockets of New York taxpayers, but is paid by the federal government in the form of lower federal tax liability for New Yorkers.



## B. Income Tax Base Broadening Options

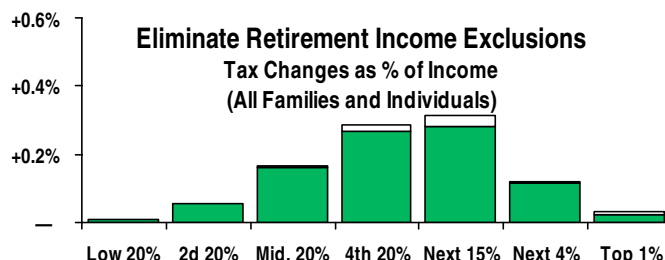
#### 6. Eliminate Retirement Income Exclusions

##### Principal Features

- Conforms the New York tax treatment of pensions and Social Security benefits to federal rules.
- Simplifies the New York tax system by eliminating two special tax preferences.
- Increases New York tax revenues by \$1.1 billion.
- Decreases federal taxes by \$86 million.

##### Discussion

This option simplifies the New York income tax by conforming to the federal income tax treatment of Social Security and pension income. New York currently exempts all Social Security income and the first \$20,000 of pension benefits. Federal income tax rules exempt all Social Security benefits for taxpayers with income below \$32,000 for married couples, and



subject less than twenty percent of elderly New Yorkers to tax on their Social Security benefits, as discussed in Chapter Four. Tying New York income tax rules to federal rules in this manner also makes the New York income tax simpler and easier to understand. Eight percent of the state tax hike from this option would be offset by federal tax cuts for New York itemizers.

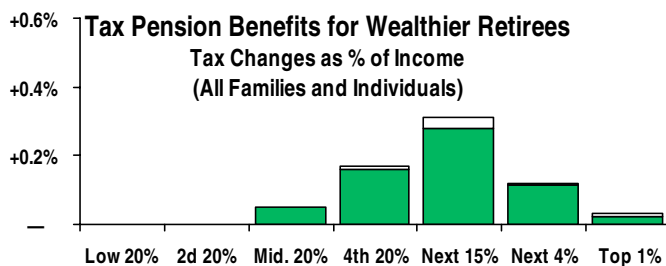
## 7. Tax Pensions for Wealthier Retirees

### Principal Features

- Adds an income limit to the current income tax exclusion for pension benefits
- Progressive tax change.
- Increases New York tax revenues by \$870 million.

### Discussion

This option disallows the pension exemption only for New Yorkers earning over \$50,000 a year. Because income taxes can be written off on federal income tax forms by itemizers, part of this hike would be offset by federal tax cuts.



## C. Better Targeting of Income Tax Credits

## 8. Limit Dependent Care Credit to Low-and Middle-Income Parents

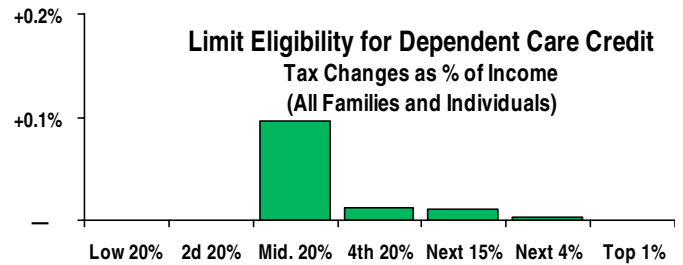
### Principal Features

- Caps eligibility for child care credit at \$40,000
- Progressive tax change.
- Increases New York tax revenues by \$90 million.

### Discussion

The New York dependent care credit is based on federal eligibility rules—which means that taxpayers at all income levels can claim the credit. Some states allowing similar credits have imposed income limits on eligibility—which better targets the credit to the low- and middle-income families who need the credit most. Because income taxes can be written off on

federal income tax forms by itemizers, a small part of this hike would be offset by federal tax cuts.



## D. New York City Income Tax Options

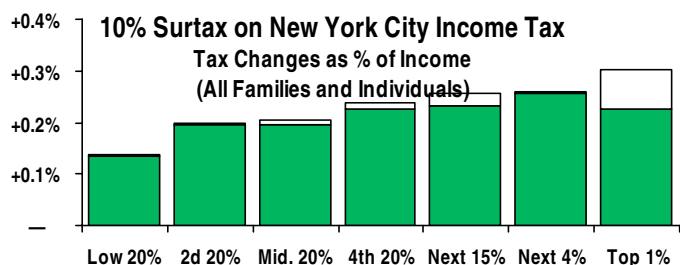
## 9. Temporary City Income Tax Surcharge

### Principal Features

- Imposes a surcharge on the City income tax.
- Progressive tax change.
- Increases New York tax revenues by \$630 million.

### Discussion

This option would impose a 10 percent surcharge on the New York City income tax. It is assumed that the 14 percent surcharge will remain part of the city income tax in 2006, but that the currently-imposed temporary top rates will expire. Because the local income tax is progressive, the surtax would be progressive too. Because local income taxes can be written off on federal income tax forms by itemizers, part of this hike would be offset by federal tax cuts.



## 10. Re-Enact New York City "Commuter Tax"

### Principal Features

- Imposes flat-rate 0.45 percent tax on New York City commuters.
- Slightly progressive tax change.
- Some of tax is paid by non-New Yorkers.
- Increases New York tax revenues by \$500 million.

## Discussion

This option recreates the flat 0.45 percent wage tax that was imposed on New York City workers living outside the city (or outside the state) from 1966 to 1999. The commuter tax ensures that workers living outside the city who commute to the city to work contribute their fair share to the cost of providing public services. Because the commuter tax was levied at a flat rate, this option is only slightly progressive. Because local income taxes can be written off on federal income tax forms by itemizers, part of this tax hike would be offset by federal tax cuts.

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## 11. New Progressive Commuter Tax

### Principal Features

- New, graduated version of commuter tax.
  - Progressive tax change.
  - Increases New York tax revenues by \$1 billion.

### Discussion

This option re-enacts the wage tax that was imposed on New York City workers living outside the city (or outside the state) from 1966 to 1999, but replaces the prior flat rate with a graduated-rate tax similar to the rate structure imposed under the city income tax (with rates substantially lower than the city rates). The commuter tax ensures that workers living outside the city who commute to the city contribute their fair share to the cost of providing services. Because local income taxes can be written off on federal income tax forms by itemizers, part of this tax hike would be offset by federal tax cuts.

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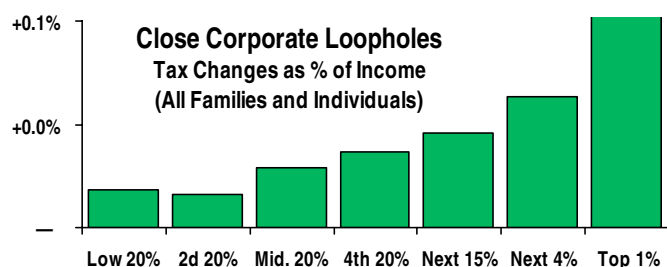
## E. Corporate Tax Reform Options

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## 12. Close Corporate Loopholes

### Principal Features

- Broadens the base of the corporate tax.
- Progressive tax change.
- Most of tax is exported to non-New Yorkers.



- Increases New York tax revenues by up to \$1 billion.

### Discussion

This option shores up the corporate tax base by strengthening the minimum tax, enacting combined reporting and a “throwback rule.” Because most of the corporate tax is exported to non-residents, the impact of this option on New Yorkers is minimal.

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## F. Sales and Transaction Tax Options

## 13. Re-enact Stock Transfer Tax At Lower Rate

### Principal Features

- Re-enacts stock transfer tax with a rate schedule one-tenth of the rates used in 1981 (when the tax was repealed).
  - Progressive tax change.
  - Much of tax is exported to non-New Yorkers.
  - Increases New York tax revenues by \$800 million.

### Discussion

This option re-creates the New York stock transfer tax, which was repealed in 1981, at a lower set of rates capped at 0.5 cents per share for the highest-valued stocks. (The original tax was levied at a rate up to ten times higher.) Because shares of stock are held disproportionately by wealthier taxpayers, this would be a progressive tax change—and because many shareholders live in other states, part of this tax hike would be exported to shareholders around the nation.

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## 14. Eliminate Sales Tax Exemptions (Services)

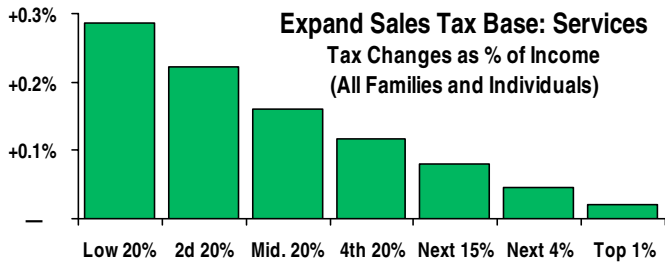
### Principal Features

- Includes certain personal services in the state sales tax base.
  - Regressive tax change.
  - Increases New York tax revenues by \$620 million.
  - Federal taxes are not affected by this change.

### Discussion

This option expands the state sales tax base by taxing various personal services, including cable TV, laundry and shoe repair, and interstate telephone service. The option would raise \$620 million for New York in 2006. Although adding services to the sales tax base makes the sales tax less regressive, the impact of this tax option is nonetheless clearly regressive compared to income- or property-tax based options. By broadening the tax base, this option treats different consumers more equally—and arguably makes it easier for lawmakers to avoid increasing the sales tax

rate. Because sales taxes are generally not deductible on federal income tax forms, little or none of this tax hike would be offset by federal tax cuts.



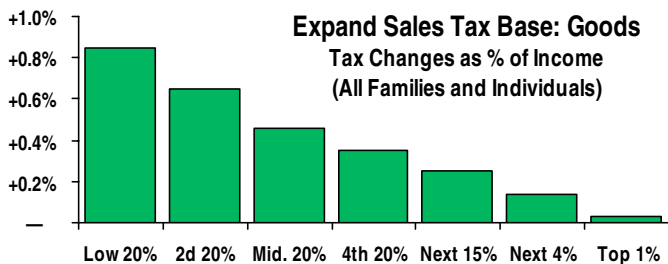
## 15. Eliminate Sales Tax Exemptions (Goods)

### Principal Features

- Eliminates exemptions for tangible property.
- Increase horizontal equity by broadening tax base.
- Regressive tax increase.
- Increases New York tax revenues by \$1.77 billion.
- Federal taxes are not affected by this change.

### Discussion

This option augments the state sales tax base by eliminating exemptions for various goods, including groceries, newspapers and periodicals, and college textbooks. This is a regressive sales tax change—but one that would yield \$1.77 billion in 2006. By broadening the tax base, this option helps to achieve horizontal equity, ensuring that the tax system won't discriminate against taxpayers based on which items they purchase—and arguably makes it easier for lawmakers to avoid increasing the sales tax rate. On the other hand, taxing “necessities” such as groceries will make the sales tax more regressive, worsening the vertical equity of the New York tax system. Because sales taxes are generally not deductible on federal income tax forms, little or none of this tax hike would be offset by federal tax cuts.



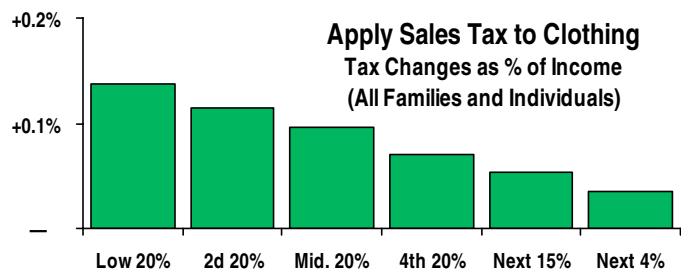
## 16. Limit Sales Tax Exemption for Clothing

### Principal Features

- Limits current sales tax exemption for sales of clothing under \$110 to two weeks per year.
- Increases New York revenues by \$520 million.

### Discussion

New York allows a state sales tax exemption for purchases of individual items worth less than \$110. (Legislation passed in 2003 temporarily suspended the exemption, but allowed a two-week sales tax holiday from the state sales tax.) The largest tax cut from this exemption, as a share of income, goes to low-income New Yorkers. This option would repeal the exemption and instead allow a two-week sales tax holiday from both state and local taxes.



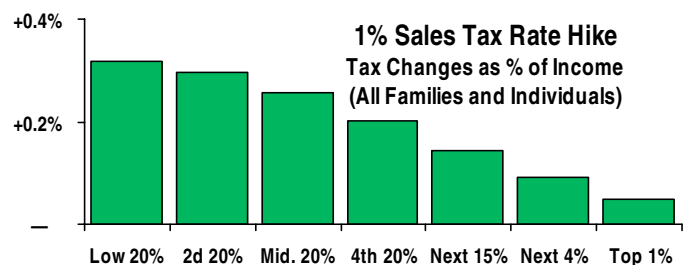
## 17. Sales Tax Rate Hike

### Principal Features

- Raises state sales tax rate by 0.5 percent.
- Regressive tax increase.
- Increases New York tax revenues by \$1.2 billion.
- Federal taxes are not affected by this change.

### Discussion

The general sales tax is the most regressive major tax levied by the state—and New York already has a relatively high state sales tax rate when local taxes are taken into account. This option would increase the state sales tax rate by 0.5 cents, raising \$1.2 billion. (2003 legislation enacted a temporary 0.25 cent sales tax increase, which is currently scheduled to sunset in



May of 2005.) Increasing the sales tax rate without broadening the tax base to include currently exempt services exacerbates the current discrimination between the low-income taxpayers who tend to consume goods and the upper-income taxpayers who are more likely to consume untaxed services. Because sales taxes are generally not deductible on federal income tax forms, little or none of this tax hike would be offset by federal tax cuts.

## 18. Expand Sales Tax Base to Include Groceries, Offer Refundable Sales Tax Credit

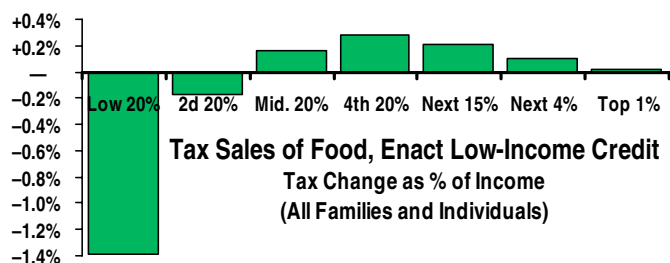
### Principal Features

- Broadens tax base by taxing groceries at the regular sales tax rate.
- Uses some revenues from this base expansion to fund a refundable tax credit designed to offset taxes on groceries; net state tax increase of \$590 million.
- Makes sales tax less regressive.
- No impact on federal income taxes.

### Discussion

This option broadens the New York state sales tax base by taxing groceries at the regular statewide rate. The sales tax hike on lower-income taxpayers is offset by a grocery tax credit designed to make the sales tax less regressive. As a result, this option would reduce taxes on low-income New Yorkers while raising \$590 million in state tax revenue. The main disadvantage of this option is the difficulty of administering a tax credit of such a large scale—and the fact that unlike the current food tax exemption, a food tax credit would only be available to those who apply for it.

Because sales taxes are generally not deductible on federal tax forms, this option does not affect federal taxes paid by New Yorkers.



## 19. Statewide Property Tax

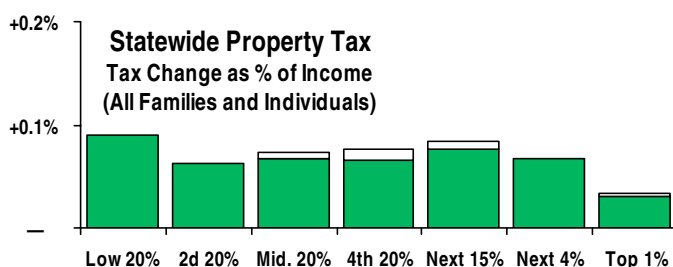
### Principal Features

- Imposes a statewide property tax.
- Regressive tax increase.
- Increases New York tax revenues by \$500 million.
- Federal taxes decrease by \$35 million.

### Discussion

This option creates a statewide property tax. This tax change would alleviate one source of tax inequity by requiring the same amount of property tax effort from the poorest and wealthiest districts. However, increasing reliance on property taxes would also make the New York tax system more regressive—and would do nothing to resolve the inequities in the current STAR exemption.

Because property taxes are deductible on federal income tax forms, some of the added property tax would be offset by federal tax cuts.



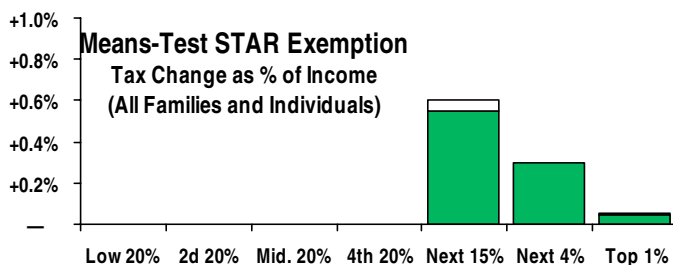
## 20. Means-Test STAR Exemption

### Principal Features

- Limits eligibility for STAR exemption to homeowners earning less than \$125,000.
- Progressive tax increase.
- Increases New York tax revenues by \$1.3 billion.
- Federal taxes decrease by \$92 million.

### Discussion

Most homestead exemptions are available to taxpayers at all income levels. But a few states now impose income limits on these exemption. This option disallows the STAR exemption for New Yorkers earning over \$125,000. Because property taxes are



deductible on federal income tax forms—and because this property tax hike would be paid almost entirely by New Yorkers who itemize and pay at higher federal income tax rates—more than 25 percent of this state tax hike would be offset by federal tax cuts.

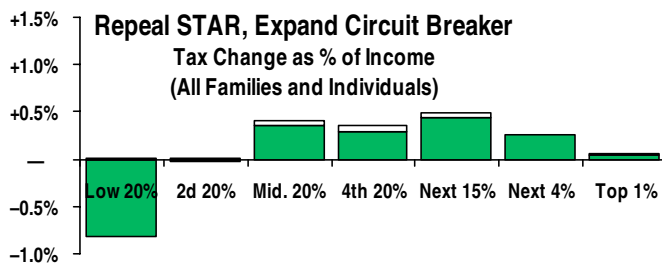
## 21. Repeal STAR, Expand Circuit Breaker

### Principal Features

- Repeals STAR homestead exemption
- Expands eligibility for circuit breaker.
- Increases New York tax revenues by \$1.6 billion.
- Federal taxes decrease by \$227 million.

### Discussion

This option repeals the STAR homestead exemption, and expands the “circuit breaker” tax credit to include more middle-income New Yorkers as well as non-elderly homeowners and renters. Because property taxes are deductible on federal income tax forms, some of this state tax hike would be offset by federal tax cuts.



## 22. Cigarette Tax Increase

### Principal Features

- Raise cigarette tax by \$0.50 per pack to \$2.00.
- Regressive tax increase.
- Increases New York tax revenues by \$250 million.
- Federal taxes are not affected by this change.

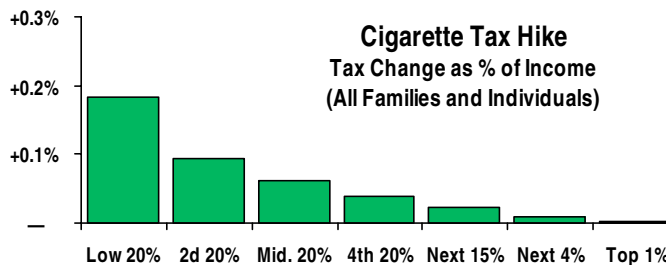
### Discussion

This option increases the state cigarette tax from \$1.50 to \$2.00 per pack. Because cigarette taxes are highly regressive, this tax hike would impact low-income taxpayers most heavily. Some argue, however, that increases in cigarette taxes may discourage smoking—although there is some evidence that high cigarette tax rates simply encourage tax evasion.

Because the behavioral effect of such a tax hike is uncertain, the actual yield of a 50-cent hike could be substantially less than the \$250 million projected here.

Cigarette taxes are a poor long-term choice for revenue raising, since they are calculated based on the volume of sales rather than as a percentage of the sales price. This means that revenues will only grow when the rate increases or when consumption grows. The recent decline in cigarette consumption means this tax is likely to decline over time.

Because excise taxes are not deductible on federal income tax forms, none of the added excise tax would be offset by federal tax cuts.



## 23. Increase Gasoline Excise Tax

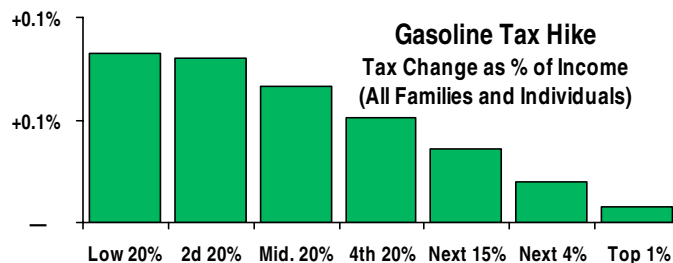
### Principal Features

- Impose 5 cents per gallon tax hike on gasoline.
- Regressive tax increase.
- Increases New York taxes by \$300 million.
- Federal taxes are not affected by this change.

### Discussion

This option would levy an additional five cents per gallon excise tax on motor fuels, with the revenues devoted to state general revenue funds. While this option is less regressive than the cigarette tax hike modeled above, this excise tax hike still hits low-and middle-income taxpayers most heavily. The “per-unit” nature of this tax means that the yield is likely to decline over time.

Because excise taxes are not deductible on federal income tax forms, none of the added excise tax would be offset by federal tax cuts.



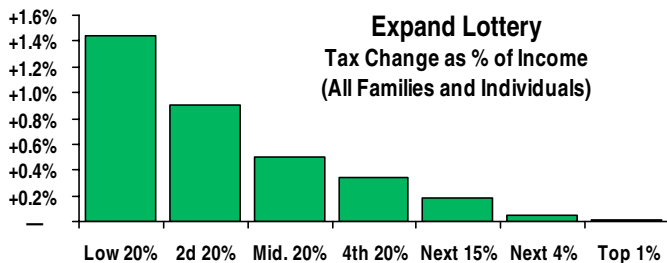
## 24. Expand New York Lottery

### Principal Features

- Increases New York revenues by up to \$2 billion.
- Federal taxes are not affected by this change.

### Discussion

Lotteries are an increasingly popular revenue-raising choice for states, and New York was one of the first states to rely heavily on this revenue source. However, a lottery is also among the most regressive revenue-raising options available to lawmakers. One recent proposal would expand the state’s reliance on “video lottery terminals” (VLTs) to fund education. Such a change could yield up to \$2 billion annually for education—although the state’s current collections from VLTs have been well below initial forecasts, and the future yield of New York VLTs could be reduced substantially if neighboring states increase their reliance on this revenue source.



## Tax Relief Options

Many of the options described in this chapter would increase taxes on low-income New Yorkers. Some options would even make the state tax system more regressive. Recognizing that lawmakers may wish to shelter low-income taxpayers from some of the additional burdens imposed through these tax increases, this section looks at several approaches to targeted low-income tax relief that could be used in conjunction with the revenue-raising options described above. Options are presented for each of the three major taxes levied in New York—personal income, property and sales taxes.

## 25. Expand the Earned Income Tax Credit

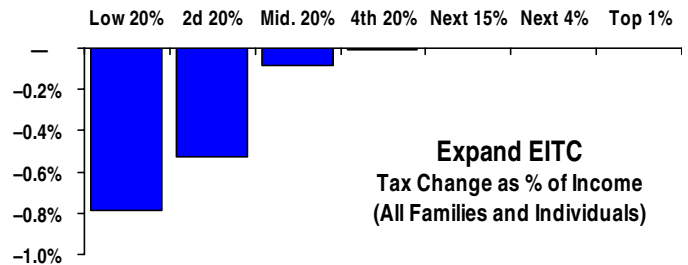
### Principal Features

- A refundable EITC based on the federal credit.
- Targeted to lower-income working families.

- Reduces New York tax revenues by \$450 million.

### Discussion

New York’s Earned Income Tax Credit (EITC) is one of the most generous in the nation—but is insufficient to offset the regressivity of other New York taxes. This option expands the state EITC to 50 percent of the federal credit, and eliminates the interaction between the EITC and the Household Credit.



## 26. Enact a \$150 Sales Tax Rebate

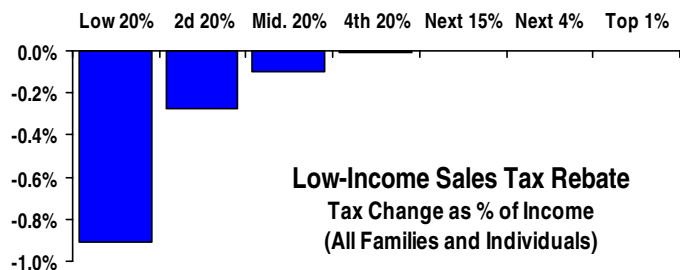
### Principal Features

- \$150 per-exemption refundable tax rebate.
- Restricted to taxpayers earning less than \$30,000 annually.
- Targeted to lower-income working families.
- Reduces New York tax revenues by \$390 million.

### Discussion

This option partially offsets the regressivity of the New York sales tax by allowing a sales tax credit for taxpayers earning less than \$50,000.

Because eligibility is limited to low-income taxpayers, the sales tax credit is a less expensive way of reducing sales taxes than an exemption. However, sales tax credits must be applied for, while sales tax exemptions are automatically granted to all eligible consumers. Low-income taxpayers who are not aware of a sales tax credit will not receive its benefits.



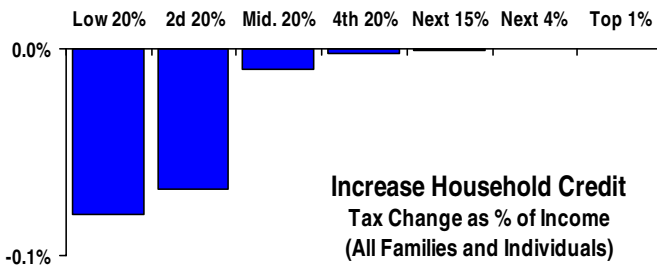
## 27. Increase Household Credit

### Principal Features

- Increases the household credit by \$50 for each family and \$25 for each exemption.
- Reduces New York tax revenues by \$55 million.

### Discussion

The New York personal exemption credit offers valuable tax relief to low- and middle-income New Yorkers. However, the credit's value has declined substantially since the credit was last adjusted in 1987. This option increases the credit by \$50 for each eligible taxpayer, plus \$25 for each exemption in the family. Because the credit is available only to lower-income New Yorkers, this tax break targets relief to the low-income New Yorkers who need it most—and results in virtually no offsetting federal tax increase.



## Putting It All Together:

As the charts at the beginning of this chapter make clear, none of the “building blocks” described so far can generate a sufficient amount of revenue to meet the *CFE* funding requirements. This section presents a variety of ways in which revenue-raising and tax-relief options could be combined to yield close to the \$8.5 billion that may be needed to comply with the *CFE* requirements. The combinations presented here are chosen to represent the variety of options available to lawmakers and should not be understood as recommendations for tax reform.

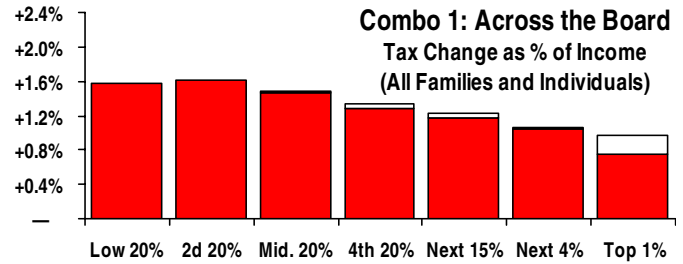
### Combination 1: Sales Tax Expansion and “Across the Board” Income Tax Hike

#### Principal Features

- Increases sales tax rate by 1 percent on all goods and expands the sales tax base.
- Increases all personal income tax rates.
- Increases New York revenues by \$8.4 billion.
- Decreases federal taxes paid by \$500 million.

### Discussion

This option takes the simplest possible approach to revenue-raising—it increases both of the major state revenue sources relied upon by New York. This plan broadens the sales tax base and increases the statewide rate by 1 percent, and increases personal income tax rates by 10 percent across the board. Even though this plan relies on the personal income tax for about half of its revenue, the net effect is slightly regressive—because the plan does not make the personal income tax more progressive.



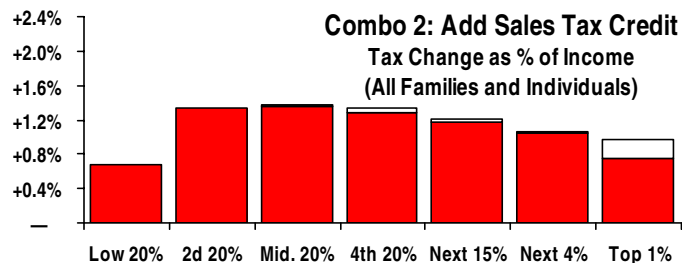
### Combination 2: Add Low-Income Relief

#### Principal Features

- Adds a Sales Tax Credit to Combination 1.
- Increases New York revenues by \$8 billion.
- Decreases federal taxes paid by \$500 million.

### Discussion

This option adds one feature to the regressive Combination 1: a \$390 million refundable sales tax credit. This addition makes this option slightly less regressive. Because the low-income beneficiaries of the sales tax credit do not itemize federal tax returns, this option results in the same federal tax change as Combination 1—yielding a greater “bang for the buck” than the first option.



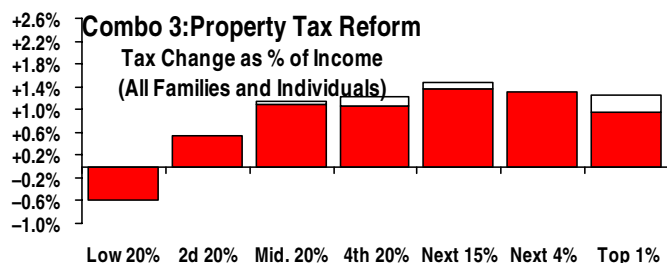
## Combination 3: Property Tax Reform

### Principal Features

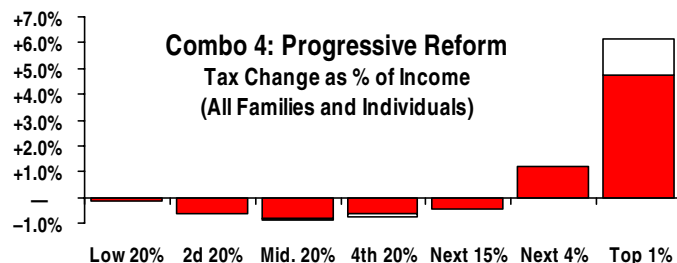
- Repeals STAR.
- Expands circuit breaker tax credit
- Enacts statewide property tax.
- “Across the board” personal income tax increase, plus corporate loophole closing.
- Increases New York revenues by \$8.5 billion.
- Decreases federal taxes paid by \$900 million.

### Discussion

This option focuses on progressive property tax reform, replacing the expensive STAR exemption with a targeted circuit breaker credit and imposing a new state-wide property tax. The option also includes the an “across the board” income tax increase and closes a variety of corporate tax loopholes. A substantial portion of this added state revenue is offset by federal tax cuts for itemizers. Because most of this plan’s revenue comes from the progressive income tax, and because the repeal of STAR makes the New York property tax much less regressive, this plan is mostly progressive overall.



New Yorkers would be offset by federal income tax cuts for New York itemizers.



## Conclusion

New York lawmakers can choose from a wide variety of tax options to achieve educational adequacy, including options that reform the tax structure and options that simply raise rates. Any revenue-raising package that fully funds education in New York will require some combination of these options, rather than relying only on one tax source.

This report does not recommend any particular option or combination of options—rather, the tax changes modeled here should be understood as representative of the range of options available to New York lawmakers.

The chart on the next page evaluates each of the options presented in this chapter in terms of the basic tax principles described in Chapter One.

## Combination 4: Progressive Tax Reform

### Principal Features

- Relies on progressive revenue sources.
- Increases New York revenues by \$8.5 billion.
- Decreases federal taxes paid by \$2 billion.

### Discussion

This option relies only on changes in the personal and corporate income taxes to raise \$8.6 billion. The option uses the 1972 income tax rates described in Option 1, and also broadens the income tax base to include retirement income for wealthier New Yorkers (leaving the retirement income of those earning less than \$50,000 a year exempt, as in Option Seven). The option also closes a variety of corporate tax loopholes. Because these taxes are federally deductible, much of the income tax increase on wealthier

## New York Tax Reform Options and Principles of Taxation

	Does Each Proposal Achieve...				
	Vertical Equity	Base- Broadening	Adequacy	Export- ability	Neutrality
<b>Revenue Raising Options</b>					
Recreate 1972 Income Tax Rates	✓		✓	✓	✓
Make 2003 Temporary Rate Hikes Permanent	✓		✓	✓	✓
"Across the Board" Income Tax Increase	✓		✓	✓	✓
"Across the Board" Tax Hike, Credit Hike	✓		✓	✓	✓
Tax Unearned Income at a Higher Rate	✓		✓	✓	
Eliminate Retirement Income Exclusions	✓		✓	✓	✓
Limit Dependent Care Credit Eligibility	✓	✓	✓	✓	✓
Temporary City Income Tax Surcharge	✓	✓	✓	✓	✓
Re-Enact New York City "Commuter Tax"	✓	✓	✓	✓	
New Progressive Commuter Tax	✓	✓	✓	✓	
Reinstate 0.5 Percent Stock Transfer Tax	✓	✓	✓	✓	
Close Corporate Loopholes	✓	✓	✓	✓	✓
Eliminate Sales Tax Exemptions (Services)		✓	✓		✓
Eliminate Sales Tax Exemptions (Goods)		✓	✓		✓
Sales Tax Rate Hike			✓		
Expand Sales Tax Base, Sales Tax Credit		✓	✓		✓
Statewide Property Tax			✓	✓	
Means-Tested STAR Exemption	✓	✓	✓	✓	
Repeal STAR, Expand Circuit Breaker	✓	✓	✓	✓	✓
Cigarette Tax Increase					
Increase Gasoline Excise Tax					
Expand New York Lottery					