OPTION:

# Cap Personal Income Tax Credit at $10,000 for Payers of the Unincorporated Business Tax

Revenue: $77 million annually

In 1966, New York City established the Unincorporated Business Tax (UBT) to tax business income from unincorporated sole proprietorships and partnerships. Since fiscal year 1997 New York City residents with positive UBT liability have been able to claim a credit against their city personal income tax (PIT) liability for some or all of the UBT they pay. The credit was created to minimize double taxation of the same income to the same individual. This option would cap the credit at $10,000 and would require state legislation.

The current PIT credit for UBT paid is designed to be progressive. New York City residents with taxable personal income of $42,000 or less receive a credit equal to 100 percent of their UBT liability. This percentage decreases gradually for taxpayers with higher incomes until it reaches 23 percent for taxpayers with incomes of $142,000 or more. Data from the city's Department of Finance on receipt of the credit by income groups shows that in 2012, more than 5,600 city resident taxpayers with federal adjusted gross income (AGI) above $1 million received an average credit of approximately $18,000. Capping the UBT credit at $10,000 would increase PIT revenue by an estimated $77 million annually. This option would not affect commuters, as they do not pay city personal income tax. Since the elimination of the commuter PIT in 1999, the UBT has been the only city tax on commuters' unincorporated business incomes earned in the city.

**Proponents might argue** that the progressive scale of the PIT credit for UBT paid is not sufficiently steep, especially at the higher income levels, and that capping the credit is a good way to control the cost of the credit to the city. They might also argue that the cap would only affect a relatively small number of taxpayers (11 percent of all UBT credit recipients), with 78 percent of those with more than $2 million in New York AGI, who would be able to afford the tax increase. There would be no reduction in the personal income tax credit provided to the other unincorporated business owners.

**Opponents might argue** that the progressive scale of the PIT credit for UBT paid means that resident taxpayers with taxable incomes over $42,000 already face some double taxation of the same income, and that double taxation would increase under the proposal. They might also argue that a better alternative would be to increase the rate on the UBT while simultaneously increasing the PIT credit for city residents' UBT liability, thereby having more of the tax increase fall on nonresidents who are not subject to double taxation on the same income by the city. As with any option to increase the effective tax on city businesses, there is some risk that proprietors and partners will move their businesses out of the city in response to the credit cap.

OPTION:

# Commuter Tax Restoration

Revenue: Over $900 million annually

One option to increase city revenues would be to restore the nonresident earnings component of the personal income tax (PIT), known more commonly as the commuter tax. From the time it was established in 1971, the tax had equaled 0.45 percent of wages and salaries earned in the city by commuters and 0.65 percent of income from self-employment. Sixteen years ago the New York State Legislature repealed the tax, effective July 1, 1999. If the Legislature were to restore the commuter tax at its former rates effective on July 1, 2016, the Mayor's Office of Management and Budget estimated that the city's PIT collections would have increased by $922 million in 2017.

**Proponents might argue** that people who work in the city, whether residents or not, rely on police, fire, sanitation, transportation, and other city services and thus should assume some of the cost of providing these services. If New York City were to tax commuters, it would hardly be unusual: New York State and many other states, including New Jersey and Connecticut, tax nonresidents who earn income within their borders. Moreover, with tax rates between roughly a fourth and an eighth of PIT rates facing residents, it would not unduly burden most commuters. Census Bureau data for 2014 indicate that among those working full-time in the city, the median earnings of commuters was $80,000, compared with $48,000 for city residents. Also, by lessening the disparity of the respective income tax burdens facing residents and nonresidents, reestablishing the commuter tax would reduce the incentive for current residents working in the city to move to surrounding jurisdictions. Finally, some might argue for reinstating the commuter tax on the grounds that the political process which led to its elimination was inherently unfair despite court rulings upholding the legality of the elimination. By repealing the tax without input from or approval of either the City Council or then-Mayor Giuliani, the state Legislature unilaterally eliminated a significant source of city revenue.

**Opponents might argue** that reinstating the commuter tax would adversely affect business location decisions because the city would become a less competitive place to work and do business both within the region and with respect to other regions. By creating disincentives to work in the city, the commuter tax would cause more nonresidents to prefer holding jobs outside of the city. If, in turn, businesses that find it difficult to attract the best employees for city-based jobs or self-employed commuters (including those holding lucrative financial, legal, and other partnerships) are induced to leave the city, the employment base and number of businesses would shrink. The tax would also make the New York region a relatively less attractive place for businesses to locate, thus constraining growth of the city's economy and tax base. Another argument against the commuter tax is that the companies that commuters work for already pay relatively high business income and commercial property taxes, which should provide the city enough revenue to pay for the services that commuters use. Finally, with the advent of the mobility payroll tax to support the Metropolitan Transportation Authority, suburban legislators could argue that suburban households (and firms) are already helping to finance the city's transportation infrastructure.

OPTION:

# Personal Income Tax Increase For High-Income Residents

Revenue: Over $500 million annually

Under this option the marginal personal income tax rates of high-income New Yorkers would be increased. Currently, there are five personal income tax (PIT) brackets. The fourth (next-to-top) bracket begins at $50,000 of taxable income for single filers, $90,000 of taxable income for joint filers and $60,000 for heads of households, and its effective marginal tax rate is 3.65 percent (the 3.2 percent base rate multiplied by the 14 percent surcharge). A fifth bracket was established in 2010 when the state Legislature eliminated STAR-related PIT benefits for all filers with taxable income above $500,000, and its marginal rate is 3.876 percent.

This option would increase current marginal tax rates by a tenth for single filers with taxable incomes above $200,000, for joint filers with incomes above $250,000, and for heads of household with incomes above $225,000. The change would effectively add a bracket in which income above these thresholds up to $500,000 would be taxed at the rate of 4.013 percent. The top bracket marginal rate would become 4.264 percent.

This option is similar in structure to the 2003–2005 PIT increase that raised upper-income tax burdens, but the rate increases kick in at higher income levels and the rates are lower than they were under the 2003-2005 increase. This option also differs from the 2003-2005 increases in that it does not include a “recapture provision” under which some or all of taxable income not in the highest brackets were taxed at the highest marginal rates. If this option were in effect for fiscal year 2017, PIT revenue would have increased by $568 million. This tax change would require approval by the state Legislature.

**Proponents might argue** that a PIT increase for high-income households would provide a substantial boost to city revenues without affecting the vast majority of city residents. Only 4.9 percent of all city resident taxpayers in calendar year 2017 would pay more under this proposal; all of them would have adjusted gross incomes above $200,000. There is no evidence that these affluent New Yorkers left the city in response to 2003-2005 tax increase, even with a larger state income tax increase also enacted at the same time. Also, this proposal avoids burdensome recapture provisions and features far smaller tax increases than those enacted from 2003 through 2005, so most of the affected taxpayers would bear less of a tax increase than they did previously. Finally, for taxpayers who do not pay the alternative minimum tax and are able to itemize deductions, increases in city PIT burdens would be partially offset by reductions in federal income tax liability, lessening incentives for the most affluent to move from the city.

**Opponents might argue** that New Yorkers are already among the most heavily taxed in the nation and a further increase in their tax burden is likely to induce movement out of the city. New York is one of only three among the largest U.S. cities to impose a personal income tax, and its PIT burden is second only to Philadelphia’s. Tax increases only exacerbate the city’s competitive disadvantage with respect to other areas of the country. Even if less burdensome than the 2003-2005 increase, city residents earning more than $500,000 would pay, on average, an additional $7,700 in income taxes in calendar year 2017. With the option, these taxpayers are projected to account for 53 percent of the city’s PIT revenue. If 5 percent of them were to leave the city in response to higher taxes, this option would yield $310 million less PIT revenue per year (assuming those moving had average tax liabilities for the group).

OPTION:

# Restructure Personal Income Tax Rates To Create a More Progressive Tax

Revenue: Over $400 million annually

This option would create a more progressive structure of personal income tax (PIT) rates by reducing marginal rates in the bottom income brackets and raising marginal rates for high-income filers. This option would provide tax cuts to most resident tax filers and a lasting boost to city tax collections.

Seven tax brackets would replace the current five brackets, with the following effective marginal rates (including the 14 percent surcharge). The income ranges of the two lowest brackets would remain the same but their marginal rates would be reduced—from 2.91 percent and 3.53 percent to, respectively, 2.33 percent and 3.18 percent. The rates and income range of the third bracket would remain the same (3.59 percent). The fourth marginal rate would remain 3.65 percent but the bracket would end at taxable incomes of $200,000 for single filers, $250,000 for joint filers, and $225,000 for heads of households. The fifth bracket would have a marginal rate of 4.01 percent for all filers with incomes up to $500,000. The current top bracket, for incomes above $500,000 would become two brackets, with a 4.26 percent marginal rate for those with incomes up to $1 million, and a 4.48 percent rate on higher incomes—increases of 0.39 and 0.60 percentage points, respectively over the current top rate. This option does not include "recapture provisions," so taxpayers in the top brackets would continue to benefit from the marginal rates in the lower brackets of the tax table.

If the new rates were approved by the state and went into effect at the beginning of fiscal year 2017, the city would have received an additional $445 million in PIT revenue in 2017.

**Proponents might argue** that a progressive restructuring of PIT base rates would simultaneously achieve several desirable outcomes: a lasting increase in city tax revenue, a tax cut for the majority of filers, and a more progressive tax rate structure. Under this restructuring option, about 67 percent of all tax filers would receive a tax cut in calendar year 2016. Restructuring would significantly heighten the progressivity of the PIT, which had become less progressive in 1996 when the number of tax brackets was reduced. Finally, they could point out that for taxpayers who do not pay the alternative minimum tax and who itemize deductions on their federal returns, increases in city PIT burdens would be partially offset by reductions in federal income tax liability.

**Opponents might argue** that if the principal goal of altering the PIT is to raise revenue, this option is very inefficient. For 2017, the reductions in marginal rates in the bottom two tax brackets decrease the revenue-raising potential of the higher marginal rates in the upper brackets by about $273 million. The tax increases in this option would be on top of the 2010 tax increase on filers with incomes above $500,000 due to New York State's elimination of STAR PIT rate cuts. Filers with incomes above $1 million would see their PIT liabilities rise on average by an estimated $23,000 in calendar year 2016. If only 5 percent of "average" millionaires (about 1,500 filers) were to leave town, this option would yield $271 million less in PIT revenue per year, and over time this revenue loss would be further compounded by reductions in other city tax sources.