

How High Is The Upstate Tax Burden – and Why?

Upstaters pay up to \$6 billion more in state and local taxes than they would in an average state. Blame Medicaid, and payrolls.

New Yorkers are well aware that this is a high-tax state. But for years, many in the Albany political community have taken comfort in the belief that this is really only a big problem Downstate – where costs of all kinds are, they think, just naturally much higher.

Unfortunately, a detailed examination of the numbers shows that Upstate's businesses and

Upstate's excess burden of state and local taxes is a significant drag on the region's economy.

taxpayers are paying state and local taxes that are about \$5 billion to \$6 billion a year higher than they would be if they were living in, say, Ohio. And that's more than enough to impose a significant drag on the region's economy – one

reason Upstate's job growth has lagged behind competing states' for so long.

According to the latest available tax data analyzed by the Public Policy Institute, state income taxes per capita in Upstate New York are about 22 percent higher than the national average – meaning Upstaters are paying about \$800 million a year above the norm.

But the disparity in **local** taxes is even higher. Property taxes per capita Upstate are about 55 percent above the national average (and compared to Ohio, say) – a total of over \$3 billion above the norm. And local sales taxes Upstate are double the national average – costing Upstaters another \$1.3 billion a year.

INSIDE

New York's chronic high-tax problem isn't just a Downstate phenomenon. It's a serious problem Upstate, too – and it won't be easy to fix:

- ◆ **Upstaters pay state and local taxes that are as much as \$6 billion a year higher than they would be if our taxes matched the national average per capita.**
- ◆ **Most of that excess is in local, not state, taxes.**
- ◆ **Local taxes are pushed up by state mandates, and by big-spending habits at the local level.**
- ◆ **The worst single mandate, Medicaid, accounts for about \$1 billion of the excess Upstate tax burden. But shifting the cost to the state would only make the Upstate tax gap worse. The only recourse is to cut the program.**
- ◆ **Some \$4 billion of the tax excess is caused by excess government jobs at the local level.**

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Taxes are higher because *spending* is higher – obviously. Two aspects of government spending Upstate particularly stand out:

1. Upstate local governments have a total of some **93,500 more employees** than they would have if we matched the national average ratio of local government workers to population – an excess of more than 25 percent. This, alone, costs Upstate taxpayers more than **\$4 billion extra** a year.
2. And New York’s **Medicaid** program costs Upstate taxpayers about **\$1 billion more** a year in state and local taxes than it would if it matched the national average per recipient.

This problem of high spending and high taxes cannot be tackled without action both in Albany and at the local level. Downsizing local governments will require serious and difficult initiatives at the local level – perhaps including significant consolidation of governmental structures, or at least of certain services. Albany, meanwhile, must reform its “mandates” – the state rules that help drive up so many costs at the local level – from Medicaid to collective bargaining to the restraints on governmental consolidation, downsizing and/or privatization.

The state-local interface

Most published comparisons of taxes and spending among the 50 states break down the figures on a state-by-state basis, rather than separating out particular regions like Upstate. The states provide statewide figures on both state and local taxes to the U.S. Census Bureau, which then corrects them for comparability. Most analysts prefer to do state-by-state comparisons using the combined impact of state *and* local taxes, because the burden of providing services is divided up in different ways in different states. On this statewide basis, New York has the highest state-local tax burden in the nation – 48 percent above the national average per capita.

But in part because Albany shifts social services costs to the localities, it is not *state* taxes that give New York its #1 ranking. The Tax Foundation, for example, ranks New York 21st in terms of state corporate tax burden, and 35th in terms of state personal income tax burden (on scales where 1 is best and 50 is worst). New York’s state sales tax rate of 4.25% is below the national median of 5%.

In local taxes, however, New York ranks 3rd in the nation for property taxes per capita (4th if ranked by property taxes per \$1,000 of personal income). New York also allows localities to levy much higher local sales taxes than are found in other states. And New York City is one of the few in the nation with a local tax on personal income. It’s this combination of high local taxes in virtually every conceivable form that makes New York #1 in overall state-local tax burden.

And what about Upstate?

Once we try to separate out the numbers for Upstate New York, we see there is a kernel of truth in the old Albany canard that New York’s high overall tax burden mostly reflects on Downstate, not Upstate. That kernel of truth is this: the burden of the state’s personal income tax is worse Downstate than Upstate. New

York's personal income tax is highly "progressive" (targeted at upper-income taxpayers), and incomes are higher in New York City and its suburbs. So state income taxes per capita are *four times* the national average in Westchester County, and three times average in Suffolk County, for example – but only 22 percent above average in Upstate as a whole.

But then consider the numbers for *local* taxes Upstate :

- Local property taxes in Upstate New York overall are about 55 percent above the national average. Ohio, to cite one state where the economy and demographics are roughly comparable to Upstate, has property taxes per capita that are slightly *less* than the national average. The 55 percent gap translates into big money – property taxes Upstate in 2001 were a total of some \$3.1 billion higher than they would have been, had they matched the national average per capita.

In Monroe County, for example, property taxes collected by all units of local government (the county, school districts, Rochester, towns, etc.) in 2001 added up to almost \$1,400 per capita – about 70 percent above the national average. Property taxes in Albany County appear to have been about 75 percent above the national average per capita. In Broome County the gap was about 46 percent; in Erie County , about 42 percent; in Onondaga County, about 48 percent; in Oneida County, about 25 percent.

- Local sales taxes Upstate are even farther above the national norm in percentage terms – although the dollar impact is less. Local sales taxes per capita Upstate were \$369 in 2001, or about 110 percent above the national average – some \$1.3 billion higher than they would have been if they had matched the national average. In Ohio, by contrast, local sales tax collections per capita were less than half the national average.*

So just these two sources of local government revenue – property taxes and sales taxes – take a combined total of almost \$4.5 billion more from Upstate taxpayers than those taxpayers would be paying if they lived in Ohio, or in some other normal state. Other state and local taxes push Upstate's excess "tax gap" to as much as \$6 billion. Where's the money going?

More than \$5 billion can be accounted for by only two things – excessive local government **payrolls** (\$4 billion +), and **Medicaid** (\$1 billion). Unfortunately, neither one has proven easy to reform.

A lot of the money goes for payroll

This part of the answer is no surprise, really. Government is a service business. Personnel is the main expense of service businesses. If government is spending too much, the first thing to check is the payroll. And employment statistics make clear that local government payrolls in Upstate New York are far out of line with national norms.

* Data for Fiscal Year 2001 from *Comptroller's Special Report on Local Government Finances for New York State*, Office of the State Comptroller, April 2003.

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New York's really big local government payroll overruns are found Upstate.

Table 1

**Where Your Tax Money Is Going
New York's high local taxes support
higher-than-average local government payrolls**

	Total jobs in local governments, 2003	Local government employees per 1,000 in (200) population
United States	13,802,000	49.04
New York State (local govt. statewide)	1,087,200	57.29
<i>If at the national average ratio to population, this number would be</i>	930,680	
<i>Excess local employment (compared to national ratio to population)</i>	+ 156,520	
Upstate New York	432,300	62.57
<i>If at the national average ratio to population, this number would be</i>	338,810	
<i>Excess local employment (compared to national ratio to population)</i>	+ 93,490	
<small>Source: U.S. B.L.S., establishment employment data, 2003 annual average, and U.S. Census Bureau. Calculations by The Public Policy Institute of New York State, Inc.</small>		

In the United States as a whole, the number of people on local government payrolls averaged 13.8 million in 2003, according to the Bureau of Labor Statistics (see Table 1). This is 49 local government employees for every 1,000 in population.

In New York State, by contrast, there were 57.3 local government employees per 1,000 population – a total of 1.08 million. That's 156,500 more than the taxpayers would be supporting if our ratio matched the national average.

(State government, in New York, by contrast, employs *below* the national norm – 13.8 per 1,000 population, versus a national average of 17.8 per thousand. This is not necessarily an unexpected sign of virtue in Albany. Large states should generally rank below average, because of economies of scale. Also, because of our superb system of private colleges, New York's state government has to staff and pay for a smaller portion of the higher education system than is true of a typical state.)

Despite their big-spending reputation, local governments Downstate average fewer employees per 1,000 population than the state average – 52 per 1,000 on Long Island, for example. Still, they are well above the national average.

The really big payroll overruns, however, are found Upstate. There, the BLS counted 432,300 local government employees or 62.57 per 1,000 population – some

25 percent above the national average. That works out to 93,500 more local government employees than there would be if Upstate matched the national average. At an estimated average cost of \$45,000 a head, this comes to an extra \$4.2 billion burden on the taxpayers.

School employees Upstate account for almost half of all local government employees in the region (211,900 of the 432,300 in the BLS count), but they account for only about a quarter (23,000) of the “excess” compared to the national average per 1,000 population. So the other three-quarters of the excess government jobs are in the myriad ranks of county, city, town and other local government units.

Clearly, therefore, **the key to closing the tax gap Upstate is to downsize local government.** But it won't be easy to do. Local payrolls got so high because it is politically more palatable to hire than to fire – indeed, many elected officials tend to think of big government payrolls as a logical way of dealing with a declining local economy. There are many impediments to consolidation and downsizing in the state Constitution and in state labor laws. Just one recent example illustrates the problem. After a horrendous local political battle, Erie County has taken over the city of Buffalo's park system. But the unions leveraged state labor laws to ensure that the deal had to be done in such a way that no one lost his job. Well, the truth is, if it doesn't cut the payroll, it probably won't save much money.

The Medicaid monster

On a statewide basis, New York's largest single state-local cost overrun (compared to the national average) is the Medicaid program. Our spending per recipient is about 64 percent above the national average. Medicaid in New York State costs about \$14 billion a year more than it would if it matched the national average per recipient – and about \$8 billion more than it would if it matched neighboring states, such as Massachusetts or Pennsylvania.*

The burden is worst Downstate; Upstate accounts for only about 22 percent of total statewide Medicaid spending even though it has 36 percent of the state's population. Still, the excess burden on Upstate taxpayers is significant. As of 2001, Medicaid spending Upstate was some \$5.6 billion – out of a statewide total (not counting state institutions) of \$25.5 billion. This is about \$2 billion more than the program would spend Upstate if New York reduced its cost per recipient to the national average. In other words, if New York held its Medicaid spending to the national average, Upstate taxpayers could save about \$1 billion in their state and local taxes (the other \$1 billion in savings going to the federal government).

An irony: a state takeover of Medicaid could cost Upstaters money

The most oft-recommended “cure” for the Medicaid burden on Upstate taxpayers is for the state government to take over the local share of the cost, thus easing the burden on the property tax. Ironically, however, this would backfire on Upstate taxpayers as a whole. Unless the program were drastically reformed first, Upstate taxpayers would end up paying at least \$250 million *more* in state taxes than they would *gain* in local tax relief.

* State-by-state data from the Kaiser Family Foundation, www.statehealthfacts.kff.org.

There are many legal and constitutional impediments to downsizing local government in New York.

If the state takes over the local share, it has to get the money from somewhere –and that somewhere is, obviously, the taxpayers.

Table 2

What a state takeover of Medicaid might mean for Upstaters
Lower property taxes; higher state taxes

\$ figures in 1,000s

The key figures for all Upstate counties combined (2001)

Property and related taxes collected BY COUNTIES	\$1,638,776
Sales and other taxes remitted to counties	1,689,678
Total county tax receipts	\$3,328,454
<i>% of county tax receipts that came from property taxes</i>	<i>50.6 %</i>
TOTAL Upstate property taxes (all levels of government)	\$8,712,826
<i>% of Upstate property taxes that go to county governments</i>	<i>18.8%</i>
Total Upstate Medicaid (federal, state, local), 2001	\$5,615,034
Share of that Medicaid cost paid through county taxes	\$815,787
<i>% of Upstate Medicaid costs paid through county taxes</i>	<i>14.5%</i>
<i>% of Upstate counties' total tax revenues that were spent on Medicaid</i>	<i>24.5%</i>
<i>% by which Upstate county property taxes would have been reduced if state took over Medicaid (and every dollar was used to cut property taxes)</i>	<i>49.8%</i>
% by which TOTAL Upstate property taxes would have been reduced by a state takeover of Medicaid (assuming money used to cut property taxes)	9.4%

Who would save what from a state takeover of Medicaid

Total statewide local share of Medicaid (incl. NYC), 2001	\$4,354,522
New York City's share of that	3,094,027
Upstate's share of that	815,787
New York City's share of total local cost of Medicaid	65.6%
New York City residents' share of state personal income tax collections	39.9%
NYC savings in local taxes, state takeover of Medicaid	\$3,094,027
NYC added PIT cost to finance state takeover	1,736,305
Net gain to NYC taxpayers, state takeover of Medicaid	+ \$1,357,722
Upstate counties' share of total local cost of Medicaid	22.0%
Upstate residents' share of state personal income tax collections	24.7%
Upstate savings in local taxes, state takeover of Medicaid	\$ 815,787
Upstate added PIT cost to finance state takeover	\$1,076,426
Net loss to Upstate taxpayers, state Medicaid takeover	– \$260,639

Sources: Data on local taxes from Comptroller's Report on Municipal Affairs for FY 2001. Data on state PIT collections from NYS Dept. of Taxation & Finance. Data on total Medicaid expenditures by county from NYS Department of Health. Data on net local share of Medicaid from New York State Association of Counties. Compilations and calculations by The Public Policy Institute. "Upstate" throughout this report refers to counties north and west of Rockland and Putnam.

How can this be? Well, if the state takes over the local share, it has to get the money from somewhere – and that somewhere is, obviously, the taxpayers. To pay for the local share, the state would either have to increase its taxes; constrain its spending on other programs (school aid, say); or (if a revenue boom somehow made it possible to pay this extra cost without increasing tax rates) shun what would otherwise be an opportunity to cut state taxes. Any way it works, the taxpayers will pay; there is no free lunch.

New York City accounts for 65.6 percent of total statewide Medicaid spending, yet for only 39.9 percent of the state’s principal tax source, the personal income tax. What this means is that a state takeover of the local share would tend to shift money to New York City, at the expense of taxpayers in the rest of the state. As of 2001, the net gain to the city would have been \$1.35 billion. (See Table 2.)

The biggest payors in this shift would be taxpayers in the affluent New York City suburbs, who bear (as noted above) a hugely disproportionate share of the state’s progressive income tax. Westchester County taxpayers, for example, would save \$128 million in local taxes but pay another \$491 million in state taxes – a net loss of \$363 million (again, based on 2001 figures, the most recent available).

Upstate, being generally less affluent than the New York City suburbs, would have a smaller – but still significant – net loss. Based on 2001 spending and tax patterns, Upstate taxpayers would pay about \$1.08 billion in state taxes to finance a state takeover, while saving about \$815 million in local taxes – for a net loss of over \$250 million. Taxpayers in Monroe County would have a net loss of \$48 million; taxpayers in Erie County would have a net loss of \$27 million. (Though a few rural Upstate counties, with high poverty ratios and few high-income taxpayers, would have at least some net benefit.)

Medicaid soaks up all the property tax? Not.

Incidentally, a state takeover of Medicaid would have less of an impact on overall property tax levels than one would think from reading all the rhetorical attention the Medicaid issue gets from Upstate elected officials.

For Upstate as a whole, Medicaid accounts for about half of all county property taxes, if one pretends that the county share of Medicaid is paid for solely by the property tax, as some county executives sometimes describe the situation. (It isn’t, of course; the Medicaid money just comes out of the general county treasury, however derived. Property taxes account for only about half of overall Upstate county tax revenues, the rest coming from sales and other taxes.)

County property taxes, in turn, account for less than 19 percent of *total* property taxes Upstate, the rest going to cities, towns, and (mostly) school districts. So as of 2001, a state takeover of Medicaid would have reduced total property taxes Upstate by just 9.4 percent – assuming the counties returned every dollar of savings to their taxpayers in the form of property tax reductions.

One possible way around this dilemma has been suggested by Erie County Executive Joel Giambra – a tax “swap” in which the state would give up a penny of its sales tax to the counties to help them pay their share of Medicaid. This

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would be enough, or nearly enough, to take care of the local share of the cost in much of Upstate. It would not, however, even come close to relieving New York City of the burden of its high-cost program. Thus his proposal would seem to have no chance of approval in the Legislature, except perhaps if tied to some alternative, large-scale transfer of state funds to the city for some other purpose – education, for example.

The only real solution to the Medicaid problem is to cut the cost, not shift it around. But that has proven to be politically very difficult. And the reason goes beyond the much-vaunted power of Dennis Rivera and the hospital workers' union concentrated in New York City. The health-care industry in every community has a powerful incentive to preserve high Medicaid spending – stronger, in a sense, than the taxpayers' drive to cut it. Look at the numbers this way. In Monroe County, to cite just one example, less than 16 percent of the cost of Medicaid is paid through local taxes (the rest being paid through state and federal taxes). What this means is that to save local taxpayers \$16, total Medicaid spending in the county has to be cut by \$100. Local health-care providers have a much stronger incentive to hang on to that \$100, than the taxpayers generally have to save their \$16. That makes Medicaid cost cuts an uphill struggle everywhere.

Solving Upstate's high tax problem requires two key things: downsizing local governments; and cutting, rather than just shifting, the cost of Medicaid. Neither step will be easy. But both are essential.