Enacted Budget Financial Plan Report

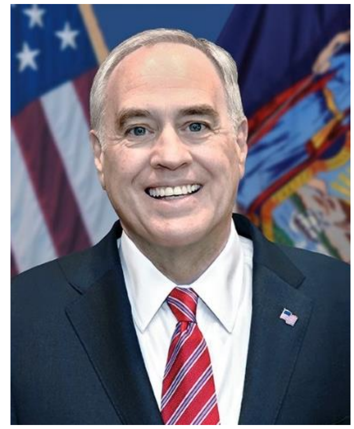
State Fiscal Year 2021-22

OFFICE OF THE NEW YORK STATE COMPTROLLER

Thomas P. DiNapoli, State Comptroller

June 2021

Message from the Comptroller



June 2021

Over the course of the last fifteen months, New Yorkers have faced unprecedented challenges from the intertwined public health and economic crises caused by the COVID-19 pandemic, and they have responded with strength and resilience.

The pandemic also created severe challenges for the State budget. One year ago, we faced the prospect of damaging mid-year spending reductions to critical programs, uncertainty about the severity and length of the economic disruption and daunting out-year budget gaps. Now, cumulative budget gaps are estimated to have fallen to $3.4 billion over the next four years.

This progress is a product of multiple factors, including a series of extraordinary federal financial assistance packages that provided historic and critically needed relief. In addition, certain sectors of our economy, notably financial services, also performed better than expected. Finally, State leaders enacted temporary new tax increases.

The improvement in the State's financial condition is encouraging. But we must remain vigilant to the risks that lie ahead and become better prepared to withstand the challenges of the future. The Financial Plan includes significant new investments to provide relief to struggling individuals and businesses, and a sustained spending increase on education; however, the Financial Plan does not make substantial investments in saving for the future. A small deposit to the State's rainy day fund reserves is planned for this year; more can and should be done to build the balances of these reserves and improve New York's ability to withstand future shocks.

This report provides information about the State Fiscal Year 2021-22 Enacted Budget Financial Plan recently released by the Division of the Budget and discusses related risks and recommendations for actions that can be taken to continue to strengthen our financial position. The Office of the State Comptroller will continue to monitor the State's financial performance as we work to support and extend the ongoing financial recovery.

Thomas P. DiNapoli
State Comptroller

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I. Executive Summary

The State Fiscal Year (SFY) 2021-22 Enacted Budget Financial Plan released by the Division of the Budget (DOB) in May 2021 details the revenue and expenditure forecast for the current and the next three State fiscal years. The Financial Plan reflects a remarkable improvement in the State's financial condition, as New York and the nation have begun to recover from the devastating impacts of the COVID-19 pandemic. Cumulative budget gaps estimated at $38.7 billion in the 30-Day Amended Executive Budget Financial Plan have now been reduced to $3.4 billion over the four-year plan.

The All Funds Budget for SFY 2021-22 totals $208.9 billion – the largest budget in State history and 12 percent greater than the prior year. This level of investment and the simultaneous reduction in forecasted budget gaps is made possible by a substantial increase in available resources over the Plan period from:

- Stronger-than-expected economic performance, which is expected to generate $20.7 billion of additional tax receipts;

- Tax increases and other policy actions approved with the Budget, which are expected to generate $17.3 billion of new revenues; and

- Federal assistance, which will provide $15.2 billion of new resources, including $12.7 billion from the American Rescue Plan and $2.5 billion from continuation of enhanced federal Medicaid cost sharing.

In addition to closing budget gaps, these resources will be used to increase local assistance program funding by over $14 billion from the Executive proposal over the Plan period, with notable investments in Foundation Aid ($11.3 billion) for school districts. Additional investments will be made in "Recovery Initiatives" that are expected to be non-recurring ($3.6 billion in State funding, in addition to $5.8 billion in federal funding). The new resources will also allow for an $825 million deposit to the State's rainy day reserve funds, and the first-ever deposits to the Retiree Health Benefits Trust Fund, totaling $640 million over two years.

While the Financial Plan outlook is markedly improved, significant underlying risks will require discipline and careful management to avoid a return to large budget gaps. A resurgence of COVID-19 or a delayed economic recovery would threaten revenue and spending forecasts; policy decisions to extend recovery initiatives beyond currently expected time frames could result in spending commitments that outstrip available resources. Increased rates on high-income taxpayers will intensify an already high level of reliance on the personal income tax as a revenue source and may make such collections even more volatile. The increased rates may also result in further out-migration of high-income taxpayers, which could significantly disrupt receipts over the long term.

To guard against these risks, policymakers should: commit to further strengthening the State's rainy day reserve funds; exercise discipline by using temporary federal resources for non-recurring obligations over the multi-year plan period; consider the long-term sustainability of major spending programs; closely monitor personal income tax collections and taxpayer behavior; and restore effective State debt management practices, including establishment of new and meaningful debt limitations and, if practicable, greater use of "pay-as-you-go" capital.

II. Financial Plan Overview

All Funds Disbursements: 12 Percent Growth

The SFY 2021-22 Enacted Budget Financial Plan (Financial Plan) released in May by DOB projects All Funds disbursements of $208.9 billion in SFY 2021-22, an increase of $22.3 billion or 12 percent over the previous year.[1] Major year-over-year increases include: $5.9 billion for school aid; $3.3 billion for Medicaid, including administration; and $3 billion for social welfare, including $2.1 billion in spending from the Department of Labor for the newly created Excluded Workers Fund, which is intended to support workers suffering loss of work-related income but ineligible for other government benefits.

These year-over-year increases are partially offset by a $6.5 billion projected decline in spending for debt service, reflecting payments made in SFY 2020-21 to repay short-term notes issued for cash flow needs ($4.4 billion) and prepayments and defeasances totaling $3.1 billion, offset by additional prepayments in SFY 2021-22 that are expected to total $1.4 billion.

Total SFY 2021-22 spending is up $12.9 billion or 6.7 percent from the 30-Day Amended Executive Budget, largely reflecting an influx of new resources from additional federal support, better-than-expected tax collections, and new taxes.[2]

All Funds Receipts: Significant New Resources Available

Total All Funds revenues are estimated to total $213.8 billion in the current fiscal year and to decrease to $199.7 billion by SFY 2024-25. As shown in Figure 1, this decline is primarily due to declining federal receipts.

Thanks to significant pandemic-related federal aid, federal receipts are projected to total $96.6 billion in SFY 2021-22, an increase of nearly $18.5 billion or 23.7 percent from the prior year. Federal aid will comprise 45.2 percent of All Funds receipts in SFY 2021-22, a significant increase from the 10-year average of 34.9 percent.

Federal relief aid from the American Rescue Plan (ARP) will total $12.7 billion and is expected to be used fairly evenly over the Financial Plan period, starting with $4.5 billion in SFY 2021-22 (5.2 percent of General Fund receipts) and ending with $3.6 billion in SFY 2024-25 (3.7 percent of General Fund receipts). Federal statute and guidance allow states wide latitude in use of these funds to provide government services and to address harmful impacts caused by the pandemic.[3]

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[1] New York State Division of the Budget (DOB), *FY 2022 Enacted Budget Financial Plan* (May 2021), available at https://www.budget.ny.gov/pubs/archive/fy22/en/fy22en-fp.pdf.

[2] References to the Executive Budget or the Executive Budget Financial Plan reflect the Budget or Plan as updated for 30-day amendments, unless otherwise noted.

[3] U.S. Department of Treasury, "Coronavirus State and Local Fiscal Recovery Funds," available at https://home.treasury.gov/policy-issues/coronavirus/assistance-for-state-local-and-tribal-governments/state-and-local-fiscal-recovery-funds.

In addition, SFY 2021-22 Medicaid spending from the General Fund will be supplemented with nearly $2.5 billion in enhanced federal Medicaid reimbursement (through the enhanced Federal Medical Assistance Percentage or eFMAP), down from $3.4 billion in SFY 2020-21. Federal education aid from three different programs will be $3.9 billion in SFY 2021-22 and total $14.2 billion over the Financial Plan. In total, pandemic-related spending from ARP and previous federal packages will total $38.9 billion over the Financial Plan period, in addition to $11.8 billion spent in SFY 2020-21.

Figure 1
All Funds Revenues, SFY 2019-20 Through SFY 2024-25
(in millions of dollars)

	ACTUAL		PROJECTED IN THE FINANCIAL PLAN				CHANGE OVER PLAN PERIOD
	SFY 2019-20	SFY 2020-21	SFY 2021-22	SFY 2022-23	SFY 2023-24	SFY 2024-25	
Personal Income Tax	53,659	54,967	61,050	65,494	68,448	71,348	10,298
Consumption and Use Taxes	18,022	16,117	18,154	19,089	19,549	20,032	1,878
Business Taxes	8,996	8,792	9,601	10,471	10,308	9,661	60
Other Taxes	2,212	2,500	2,288	2,410	2,525	2,649	361
Total Tax Collections	**82,889**	**82,376**	**91,093**	**97,464**	**100,830**	**103,690**	**12,597**
Miscellaneous Receipts	29,466	30,772	26,052	26,598	26,314	25,958	(94)
Federal Receipts	65,080	78,152	96,645	76,322	71,721	70,054	(26,591)
Total Revenues	**177,435**	**191,300**	**213,790**	**200,384**	**198,865**	**199,702**	**(14,088)**

Sources: Division of the Budget, Office of the State Comptroller

All Funds tax collections for SFY 2021-22 are projected to total $91.1 billion, growing to $103.7 billion in SFY 2024-25, due to stronger projected economic growth and tax rate increases. The Financial Plan raises revenue projections from the 30-Day Amended Executive Budget Financial Plan estimates by $20.7 billion over four years, including $4.1 billion in SFY 2021-22.

The Enacted Budget includes provisions that DOB expects will result in a net revenue increase of $3.65 billion in SFY 2021-22 and a total of $17.3 billion over the Financial Plan period, as shown in Figure 2. The most notable revenue increases are from higher PIT rates imposed on taxpayers with incomes in excess of $1.1 million and increased corporate franchise tax rates.

Top Personal Income Tax Rates

The new top PIT rates are projected to generate $2.8 billion in SFY 2021-22, growing to $4.5 billion in SFY 2024-25. These rates will increase from 8.82 percent to as much as 10.90 percent, as shown in Figure 3. The change will be in effect for tax years 2021 through 2027; starting in 2028, the rate will revert to 8.82 percent.

Figure 2
Enacted Budget Revenue Actions, SFY 2021-22 Through SFY 2024-25
(in millions of dollars)

	SFY 2021-22	SFY 2022-23	SFY 2023-24	SFY 2024-25
Personal Income Tax	**2,753**	**2,864**	**3,025**	**4,050**
Increase of Top PIT Rates	2,753	3,251	3,439	4,472
Deduction for COVID-19 Death Benefits	-	(5)	-	-
Extension of Farm Workforce Retention Credit	-	-	(11)	(11)
Real Property Tax Credit	-	(382)	(403)	(411)
Consumption/Use Taxes	**15**	**110**	**154**	**241**
Excise Tax on Adult-Use Cannabis	20	115	158	245
Extension of Alternative Fuels Tax Exemption	(3)	(4)	(4)	(4)
Extension of Sales Tax Exemption on Vending Machine Sales	(2)	(1)	-	-
Business Taxes	**774**	**1,083**	**760**	**(23)**
Increase of Corporate Franchise Tax Rates	750	1,073	796	-
Decoupling from Federal Opportunity Zones Program	44	62	44	44
Expansion of Excelsior Jobs Program to Include Child Care Services	-	-	(5)	(5)
Increase of Historic Properties Credit for Small Projects	-	-	(5)	(5)
Extension of Low Income Housing Tax Credits	-	(8)	(16)	(24)
Pandemic Recovery and Restart Program Tax Credits	(20)	(40)	(50)	(25)
Extension of Musical and Theater Production Credit	-	(4)	(4)	(8)
Miscellaneous Receipts	**106**	**366**	**474**	**502**
Mobile Sports Wagering	99	357	465	493
Allowance of Certain Lottery Game Drawings Twice a Day	7	9	9	9
All Other Revenue Actions	**2**	**2**	**-**	**1**
TOTAL ALL FUNDS IMPACT OF REVENUE ACTIONS	**3,650**	**4,425**	**4,413**	**4,771**

Source: Division of the Budget

Figure 3
New Personal Income Tax Brackets
Effective Tax Year 2021

Tax Rate	Filing Status	Taxable Income
9.65%	Single	$1.1 Million - $5 million
	Married, Joint	$2.2 Million - $5 million
	Head of Household	$1.7 Million - $5 million
10.30%	All Filers	$5 million - $25 million
10.90%	All Filers	Over $25 million

Source: NYS SFY 2021-22 Enacted Budget Revenue Article VII Bill (S.2509-C/A.3009-C)

Based on preliminary data for taxable income in the 2019 tax year, the new tax rates are estimated to impact just over 60,400 New York State personal income taxpayers with taxable income of at least $1.1 million, less than 1 percent of all taxpayers. Figure 4 shows the approximate number of taxpayers at the new tax rates.

Figure 4
Estimated Number of Taxpayers Affected by New PIT Rates by Resident Status

New PIT Rate	Resident	Part-Year/ Non-Resident	Total
9.65 percent	20,643	21,981	42,624
10.30 percent	5,093	7,309	12,402
10.90 percent	1,874	3,501	5,375
Total Impacted Taxpayers	**27,610**	**32,791**	**60,401**

Sources: NYS Department of Taxation and Finance, Office of the State Comptroller analysis

Corporate Franchise Tax Rates

The tax rate for the net income base of the corporate franchise tax will be increased from 6.5 percent to 7.25 percent on businesses with incomes over $5 million. Businesses which determine their tax liability using their capital base (rather than net income or fixed dollar minimum bases) will have their rates increased from 0.025 percent to 0.1875 percent. Small businesses will have a capital base tax rate of 0 percent. Increased tax rates will be in effect for tax years 2021 through 2023. In 2024, the capital tax rate will revert to 0 percent, the tax rate that would have previously been in effect starting in tax year 2021.

See the Appendices for a comparison of Receipts and Disbursements from SFY 2020-21 to SFY 2021-22 for the General Fund, State Operating Funds, All Funds, and Federal Funds, along with Financial Plan projections through SFY 2024-25.

Substantial Investments, Minimal Savings

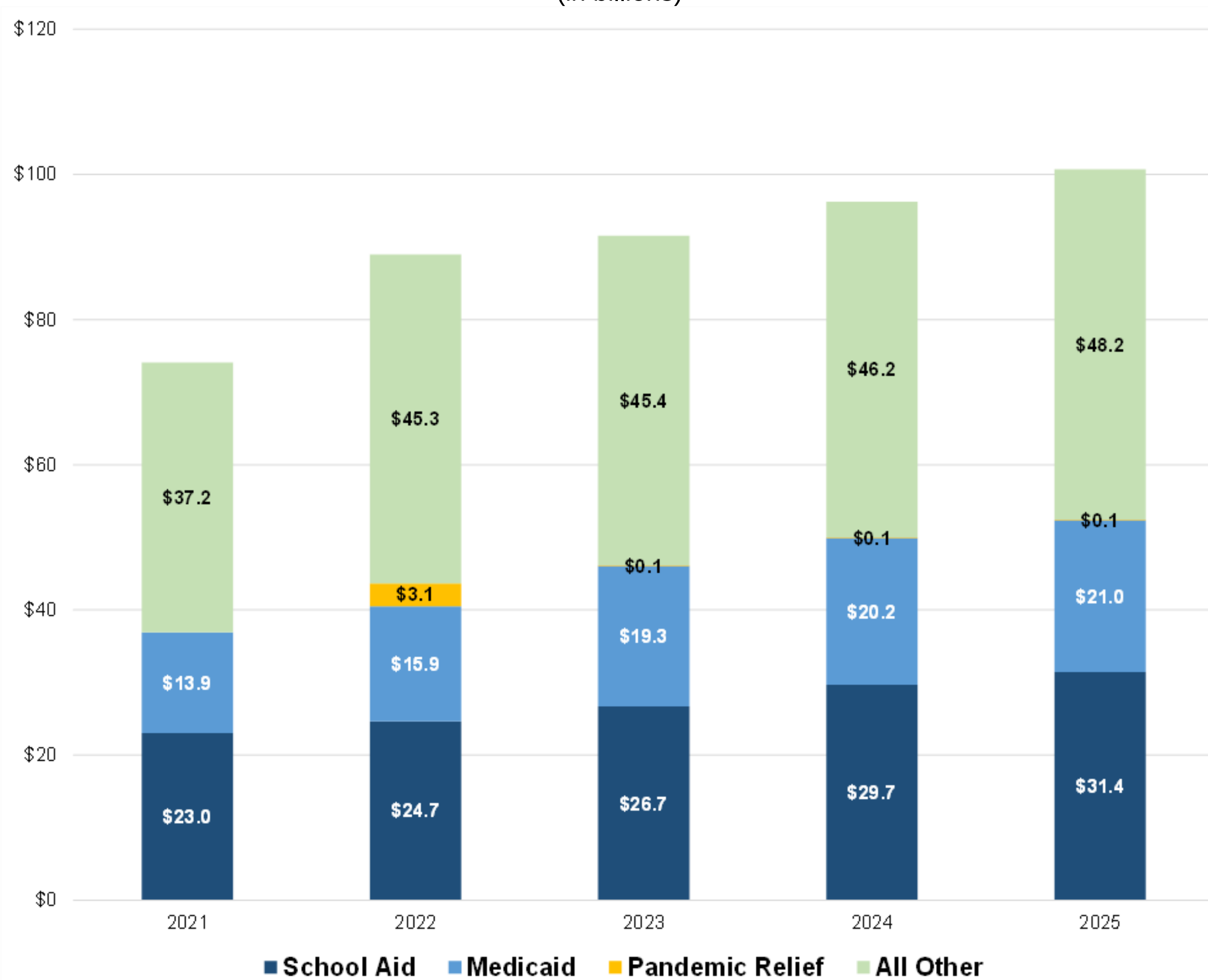
All Funds spending is projected to decline from $208.9 billion in the current year to $202.7 in SFY 2023-24 as federally funded spending ends. The current year includes $16.4 billion in COVID-related assistance (including aid enacted before SFY 2021-22), of which $13.2 billion is funded with federal dollars. Federally funded pandemic relief is expected to decline to $1.7 billion by SFY 2024-25. All Funds spending is expected to increase slightly in SFY 2024-25, primarily due to increases in State-funded Medicaid and school aid.

Most pandemic-related spending is backed by federal funds and is anticipated to be temporary. For example, over the life of the Financial Plan, such spending includes: $1.6 billion in new Medicaid spending for home and community-based or other approved services; $2.75 billion for emergency rental assistance; $2.4 billion for child-care services; and $2.2 billion for small business recovery grants. These programs are discussed in more detail in the “Risks to the Financial Plan” section of this report.

General Fund spending is projected to increase 20.1 percent in the current year to $89 billion and to grow 4.2 percent annually on average over the rest of the Financial Plan. As shown in Figure 5, the Plan includes nearly $3.1 billion in State pandemic-related aid programs not supported with federal assistance in the current year, including most notably $2.1 billion for the Excluded Workers program and $865 million for small business relief. Fiscal recovery funding from the federal government is also expected to support another $6.8 billion in General Fund spending, including $4.5 billion from the American Rescue Plan and $2.3 billion from the Coronavirus Relief Fund (CRF) enacted with the CARES Act.

State-funded pandemic relief initiatives are anticipated primarily in the current fiscal year, with little planned for subsequent years. However, significant new recurring spending commitments are planned, particularly in two key areas: education and Medicaid. General Fund spending in these areas is projected to increase by more than $15 billion over the Financial Plan period, comprising more than 58 percent of total growth in General Fund spending over that time.

Figure 5
General Fund Disbursements, SFY 2020-21 – SFY 2024-25
(in billions)



Note: “All Other” change between SFYs 2020-21 and 2021-22 includes growth in the following program areas that are offset with other changes: $2.6 billion in Mental Hygiene; $2.3 billion of “all other” local assistance; $2.3 billion in State Operations; and $1.4 billion in General State Charges.

School aid is primarily made up of Foundation Aid, a needs-based formula grant intended to allow all school districts to meet the State's constitutional mandate to provide a "sound, basic education." The Enacted Budget includes a plan to fully fund Foundation Aid according to the current formula within the next three years, a commitment expected to cost approximately $1.4 billion annually. If increases are spread evenly over the next three years, this would increase education costs by $4.2 billion in SFY 2023-24. DOB projects total school aid (including Foundation Aid and other expense-based aids) to reach $31.4 billion in SFY 2024-25, an increase of $6.7 billion from the current year, reflecting average growth of 8.4 percent annually.

Costs are increasing in the Medicaid program due to higher-than-anticipated enrollment, primarily in managed care and long-term managed care programs. DOB has steadily increased projections for General Fund Medicaid spending associated with enrollment; from 30-Day Amended Financial Plan levels, the Financial Plan adds $256 million to the current year and $236 million in SFY 2022-23. Currently, DOB projects General Fund Medicaid spending will increase by an average of 9.7 percent annually over the Financial Plan period.

In contrast to these significant new investments, modest increases are planned for State reserve funds. The Financial Plan anticipates combined total deposits of $825 million to the Tax Stabilization Reserve Fund and the Rainy Day Fund in SFY 2021-22, bringing total rainy day reserves to $3.3 billion. In addition, the State will make $640 million in deposits to the Retiree Health Benefits Trust Fund over two years. The Trust was authorized in SFY 2017-18 to dedicate resources to fund health benefits of State retirees and their dependents; unlike pensions, these benefits are not actuarially funded, but paid on an as-you-go basis. The deposits will be the State's first to the Fund.

Spending Trajectory and Out-Year Gaps

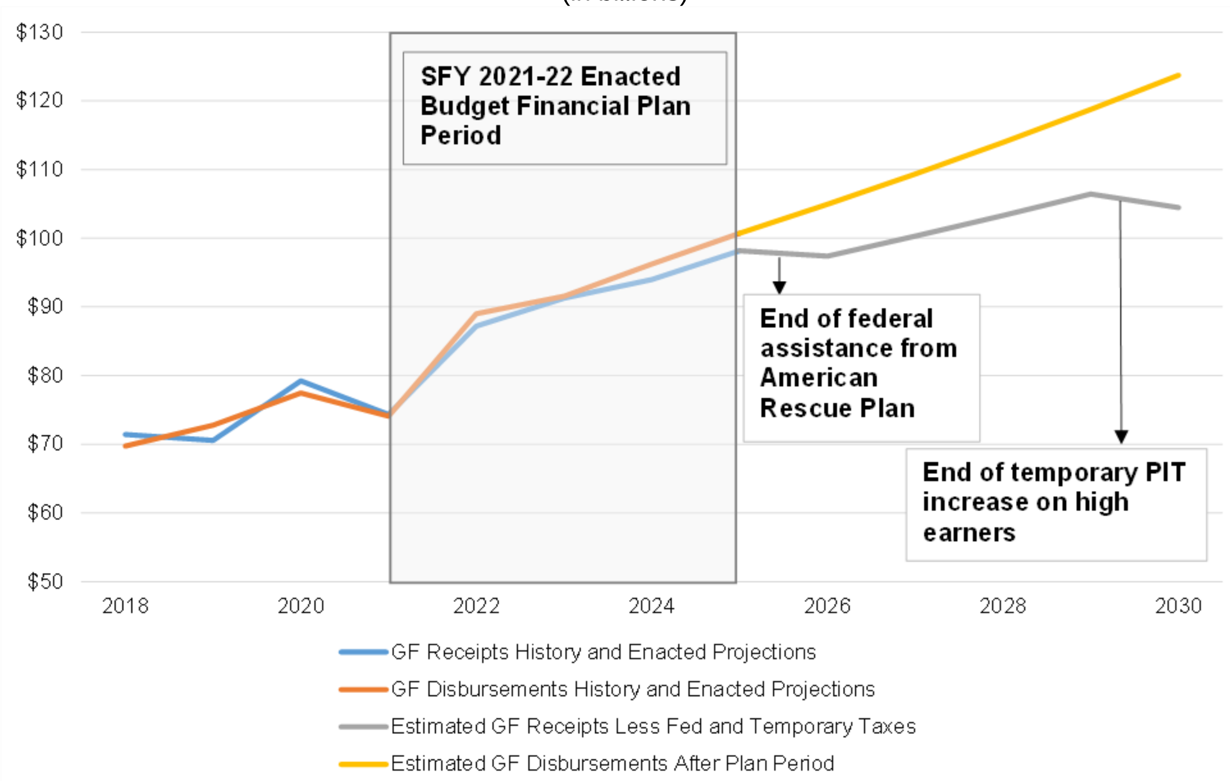
The 30-Day Amended Executive Budget Financial Plan presented budget gaps totaling $38.7 billion over four years. The Enacted Budget Financial Plan eliminates gaps in SFYs 2021-22 and 2022-23 and reduces cumulative gaps in SFYs 2023-24 and 2024-25 to $3.4 billion.

Figure 6 illustrates projected General Fund spending and receipts over the Enacted Budget Financial Plan period, and shows how the General Fund gaps may increase in the subsequent period if spending continues to grow on the trajectory currently projected in the Financial Plan, approximately 4.0 percent annually after SFY 2022-23.

The gaps grow as non-recurring revenues, including receipts from new PIT rates on high income taxpayers, corporate tax increases, and federal assistance, are depleted or expire. Unrestricted federal assistance from the American Rescue Plan ends in SFY 2024-25, and enacted corporate tax and PIT increases expire on December 31, 2023 and December 31, 2027, respectively.

In the five years following the current Financial Plan period, budget gaps would increase from nearly $8 billion in SFY 2025-26 to nearly $20 billion in SFY 2029-30 if spending and receipts were to continue on the trajectory forecast.

Figure 6
General Fund (GF) Actual and Projected Receipts and Disbursements
SFY 2017-18 through SFY 2029-30
(in billions)



Sources: Division of the Budget, Office of the State Comptroller

III. Risks to the Financial Plan

The influx of substantial new resources into the Enacted Budget Financial Plan is projected to support significant new spending and improve structural balance; however, there are a number of risks associated with any long-term financial plan, especially one that must be implemented during a period of ongoing uncertainty, as the State and its local governments manage a recovery in the wake of devastation caused by the COVID-19 pandemic.

Spending Risks

Significant short-term investments and programs were established in the Enacted Budget to aid struggling individuals, families, and businesses in New York. State agencies are working to implement these programs and direct funding to eligible recipients, but it is too early to know to what extent these programs will prove effective. The potential need to continue to make investments in support of recovery by individuals and businesses may produce pressure to continue spending at the elevated levels established in SFY 2021-22. Notable spending increases that may be difficult to wind down include:

- $2.4 billion in additional federal resources to expand child care access in New York, lower costs to families, and help child care providers recover from the pandemic. The funding includes: up to $1.2 billion to stabilize child care providers currently operating or closed due to the public health emergency; $225 million to supplement existing local, State and federal child care subsidies; $192 million to limit co-pays for families receiving subsidies to no more than 10 percent of their income above the federal poverty level; and $100 million to expand child care capacity in areas of the State with an insufficient supply of available child care.

- $2.35 billion of federal funds for emergency rental assistance, as well as $100 million in supplemental State funds for costs exceeding federal funding or for landlords or households with priority populations and incomes exceeding statutory limits.

- $2.2 billion of State ($1.6 billion) and federal ($600 million) funding to support small businesses suffering from the COVID-19 pandemic.

- $2.1 billion in General Fund support for payments to “excluded workers” who have suffered a loss of work-related income due to the pandemic and who are not eligible for unemployment insurance benefits or federal assistance payments due to their immigration status or other factors.

- $1.6 billion of Medicaid funding made available by a 10-percentage point increase in the federal medical assistance percentage for home and community-based services, or other approved services defined in the ARP. States are required to use these funds to supplement the level of State funds spent on home and community-based services for eligible individuals through programs in effect as of April 1, 2021.

- $600 million to the Homeownership Relief and Protection program. The program will provide homeowners with assistance to prevent mortgage deficiencies, defaults, foreclosures, loss of utilities or home energy services, and displacements of homeowners experiencing financial hardship after January 21, 2020.

In addition to new State spending for education, three federal assistance programs will provide $14.7 billion in additional resources to local educational agencies over the Financial Plan period, including $3.9 billion expected to be disbursed in SFY 2021-22. These programs cover a number of pandemic-related needs, as well as costs associated with high-needs districts and students. There could be a demand for State funds to replace federal assistance when it ends.

On a combined basis, these recovery initiatives and temporary federal education resources total $6.5 billion of average annual spending, which could not be supported with currently forecast resource levels during the Financial Plan period. Beyond the Plan period, the shortfall would grow when resource levels decline due to the sunset of temporary tax actions.

In addition to these recovery initiatives, the Financial Plan forecasts significant growth in the two largest areas of State spending: Education and Medicaid. These two areas comprise approximately 50 percent of General Fund spending.

- *School Aid* – Plans to fully fund Foundation Aid are projected to increase annual spending by more than $4 billion annually by school year 2023-24. However, it is not clear what will happen after Foundation Aid is fully phased-in. The annual appropriation has generally reflected a percentage increase from the previous year instead of what the formulas would specify. In addition, Foundation Aid makes up approximately 67 percent of total school aid. Other expense-based aids also increase annually. While the growth in school aid is limited to the 10-year rolling average increase of personal income measured in the State, it has frequently exceeded that measure in enacted budgets.

- *Medicaid* – Growth in Medicaid, including from costs associated with managed long-term care, minimum wage increases and distressed hospitals, exceeded projections, leading to the deferral of $1.7 billion in State-funded payments to providers (approximately $3.5 billion total) from SFY 2018-19 into the following year, a practice which has continued ever since, including in the current year. The practice allowed the State to report that it was in compliance with the Medicaid Global Cap, which is intended to limit certain Medicaid expenses to the ten-year rolling average growth of the medical component of inflation. While spending reductions have been enacted since then, DOB has had to increase spending projections twice in the last year for SFYs 2021-22 and 2022-23 because of higher than anticipated enrollment. It is unclear if, and when, cost and enrollment pressures will subside in the Medicaid program.

In addition, the State has received and will continue to receive eFMAP through at least December 2021, reducing General Fund costs by more than $5.9 billion (about 13 percent of General Fund Medicaid spending). Beginning in calendar year 2022, the State will resume responsibility for its traditional share of costs, 50 percent, up from 43.8 percent under eFMAP.

In addition to these spending risks, the Enacted Budget includes provisions that will add costs in the future. More than $22 billion in new bonding authorizations were added; new bond issuances are now expected to exceed $45 billion through SFY 2025-26. For the second year in a row, new debt issuances were excluded from the provisions of the Debt Reform Act of 2000 that limit debt outstanding and debt service (debt issued after the current year will once again be subject to debt caps), as well as from the requirement that debt be used only for capital purposes.[4] Combined, over $20 billion in debt issuances will be excluded from the State's debt limits over SFYs 2020-21 and 2021-22, rendering the cap functionally meaningless. This will also lead to growing debt service costs to be repaid from operating revenues; debt service costs are expected to exceed $8.5 billion in SFY 2024-25.

Revenue Risks

Exclusive of federal receipts, All Funds tax revenues are projected to increase by $12.5 billion over the life of the Financial Plan. Most of these new revenues are scheduled to sunset: the three-year increased tax rates under the corporate franchise tax will expire beginning in 2024 and the temporary PIT surcharge on high-income taxpayers will expire at the start of 2028.

Other new resources include those from excise taxes on adult-use cannabis and gross gaming taxes on mobile sports betting. While collections from these new taxes are recurring, both are reliant on the establishment of new markets and consumer demand for those products. Depending on the difference between actual participation and DOB's underlying assumptions, collections could be lower than projections. This is especially true of the expected revenue from mobile sports betting. In addition to the uncertainty relating to the participation rate, the tax rate on the gross gaming revenue has yet to be determined but will instead be finalized through the process of licensing the platform providers. If the assumed tax rates do not materialize, collections could be less than the $500 million projected for when the gaming platforms are fully effective.

Changes in economic conditions, both nationally and statewide, are an inherent risk to the State's revenues. A slow recovery from the pandemic, a resurgence in virus cases, or an unrelated economic downturn can adversely impact employment and income, consumer spending, corporate profits, and a variety of other economic factors. While recent forecasts from DOB, as well as other economists, show strong growth in both 2021 and 2022, a slower economic rebound would reduce collections over the course of the Financial Plan.

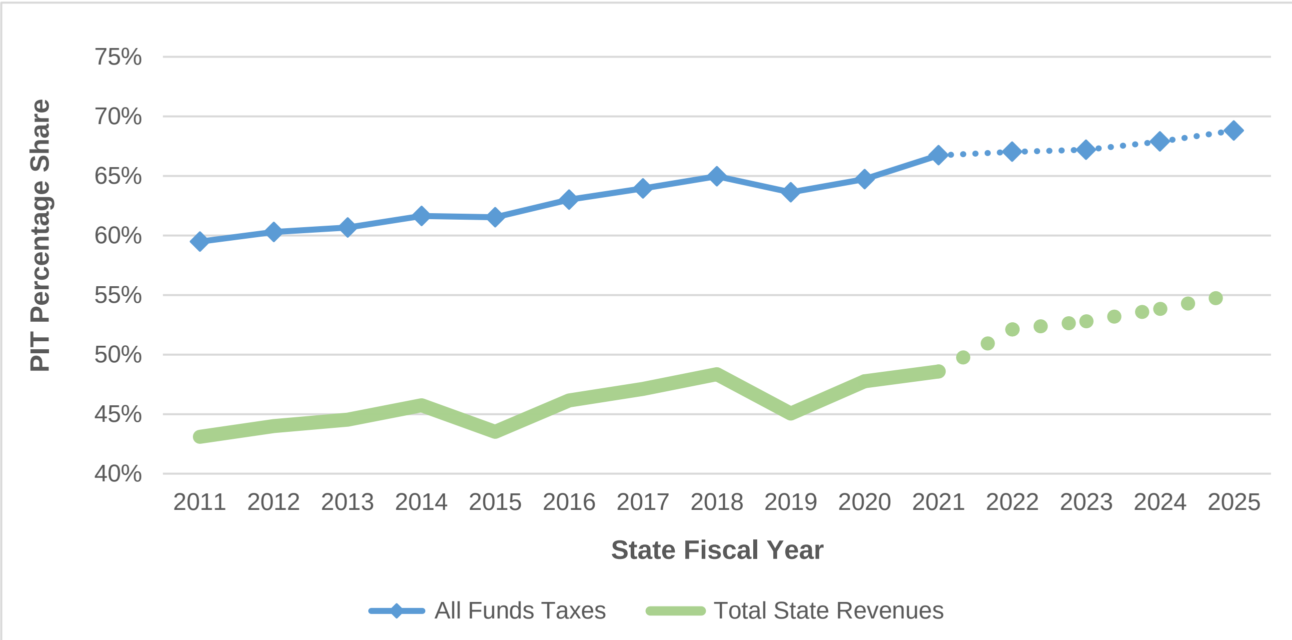
Personal Income Tax Risks

Over the past ten fiscal years, the State budget has been increasingly dependent on PIT revenues, rising from 59.5 percent of total tax revenues in SFY 2010-11 to 66.7 percent in SFY 2020-21, as shown in Figure 7. As a share of total State revenues, PIT collections increased from 43.1 percent to 48.6 percent over the same period.[5] The PIT as a share of total tax revenues is projected to near 70 percent by the end of the Financial Plan period, comprising 55 percent of total State revenues.

[4] In addition, bonds issued by the State on behalf of the Metropolitan Transportation Authority were permitted to have terms up to 50 years, instead of 30 years.

[5] For purposes of this section, State revenues are total All Funds revenues less federal receipts.

Figure 7
Personal Income Tax Collections as a Share of All Funds Tax Revenues and Total State Revenues, SFY 2010-11 Through SFY 2024-25



Note: Dotted lines are projections.
Source: Division of the Budget, Office of the State Comptroller analysis.

Compounding the State's high reliance on this revenue source is a significant dependence on a small number of taxpayers for a large share of PIT revenue. From tax years 2015 to 2019, 1.1 percent of taxpayers, on average, had taxable incomes over $1 million; however, these taxpayers paid an average of 40 percent of the State's PIT liability, or approximately $18.3 billion. The Enacted Budget Financial Plan relies on an additional $2.7 billion in personal income tax revenues from these high-income taxpayers in the current fiscal year, growing to $4.5 billion by SFY 2024-25, resulting in a higher reliance on this small taxpayer population.

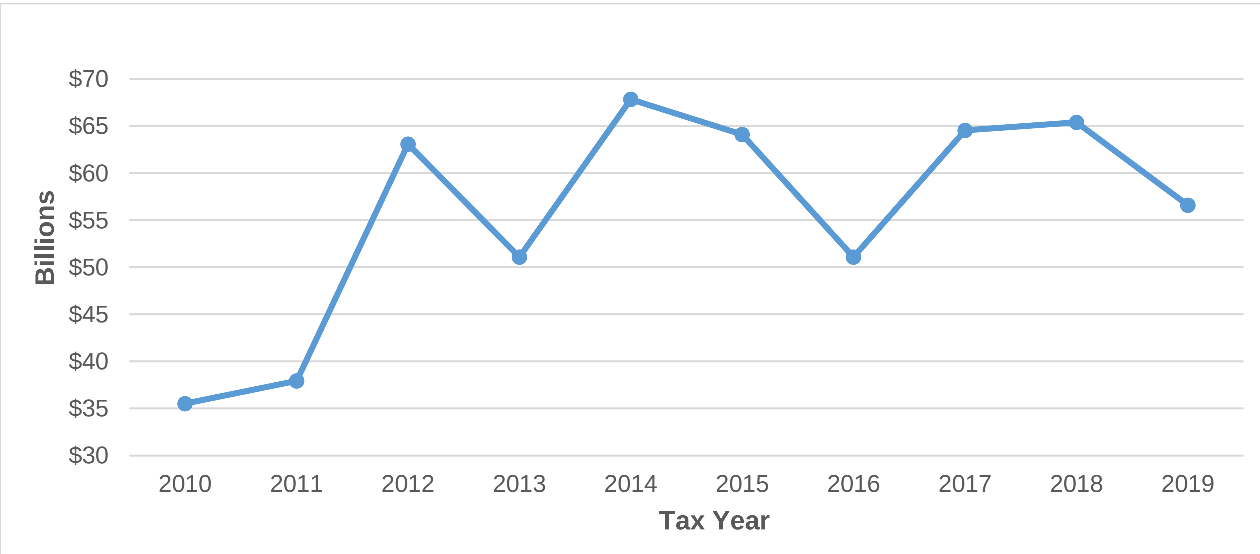
High-income taxpayers generally receive a large share of their income from very volatile income sources, especially from capital gains. Based on the latest data available, capital gains from taxpayers with incomes over $1 million comprised nearly three-quarters of the total reported by all New York taxpayers.[6] In addition, from 2010 to 2019, capital gains accounted for just over 30 percent, on average, of total income received by resident taxpayers at this income level.

Figure 8 shows how the income from the net capital gains reported by these high-income taxpayers has fluctuated annually over the past decade. While some of the fluctuation can be attributed to financial market performance, these taxpayers also have flexibility with the realization of some of this income. For example, capital gains spiked in 2012 as taxpayers

[6] New York State Department of Taxation and Finance, Tax Year 2019 Preliminary PIT Study File.

sought to avoid the rate increases associated with the expiration of lower federal tax rates on January 1, 2013.

Figure 8
Net Capital Gains Reported by New York Residents with Incomes Over $1 Million, Tax Years 2010 Through 2019



Source: U.S. Internal Revenue Service, NYS Department of Taxation and Finance

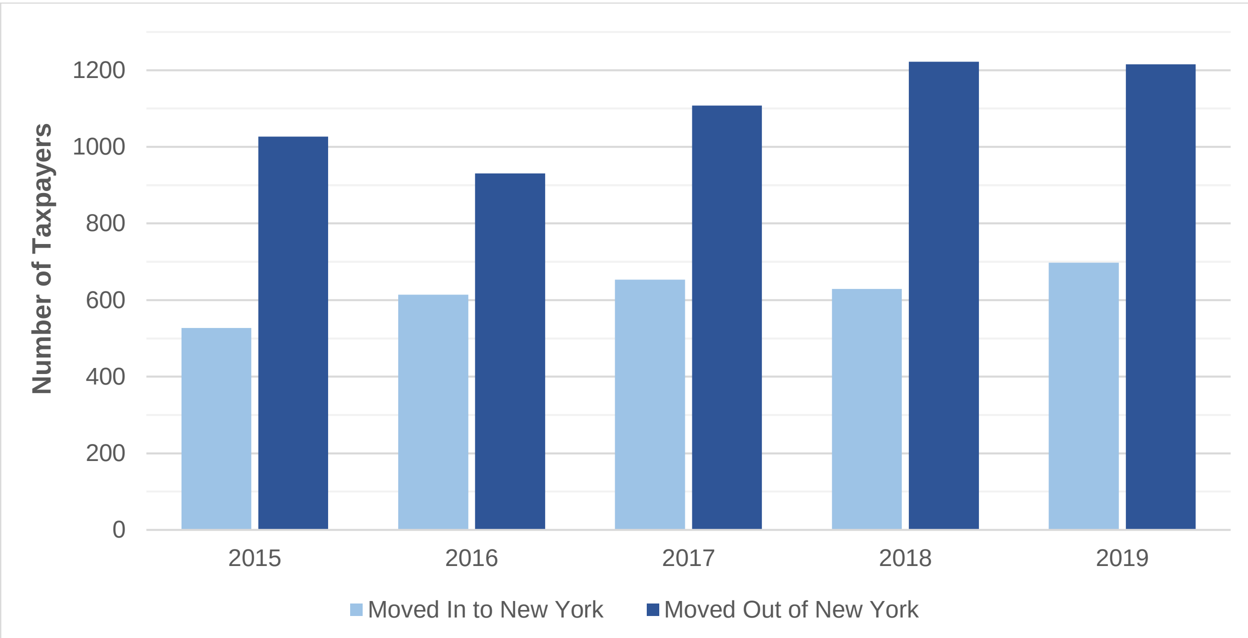
As noted, large changes in capital gains reported by these high-income taxpayers result in similar differences in the amount of PIT revenues collected by the State. The 13.5 percent decrease in capital gains reported in 2019 contributed to a $260 million decline in PIT collections that year.

DOB's revenue projections also depend on high-income taxpayers continuing to be New York residents. The recent increases to bring the top State PIT rate to 10.9 percent make the State's rate third highest in the country, and the highest among its neighboring states. Top rates in New Jersey and Connecticut are 10.75 percent and 6.99 percent, respectively.

Combining State rates with the top New York City PIT rate of 3.876 percent results in the highest top PIT rate –14.78 percent – in the nation. The top rate in California, which now will be the nation's second highest, is 13.30 percent. While there has been mixed evidence on migration in response to tax increases in the past, the rates for New York City-based taxpayers will be higher than ever before and come on the heels of a prolonged period of remote work. The potential for remote work to become more common when the pandemic is over also increases the risk that some high-income taxpayers, over the long term, may respond to tax increases by changing their state of residence.

Increasing numbers of high-income earners were leaving New York even before recent tax changes. As shown in Figure 9, between tax years 2015 and 2019, a consistently larger number of taxpayers with incomes over $1 million left New York compared to those who moved in, constituting a net out-migration of 1 percent of such taxpayers annually on average.

Figure 9
New York Taxpayer Migration, Incomes Over $1 million, Tax Years 2015 - 2019



Source: NYS Department of Taxation and Finance

A continued 1 percent decrease in the number of these high-income taxpayers would potentially result in a loss of $1.1 billion in taxable income and a reduction in PIT revenues by over $108 million, annually.[7] Moreover, the new tax rates may motivate a higher number of taxpayers to leave New York or reduce those who decide to relocate here. For example, an out-migration of 2 percent of the State's high-income taxpayers could potentially result in a loss of $2.5 billion in taxable income, or $248 million in annual tax revenue.

While the higher tax rates are temporary, sunsetting at the end of 2027, the top rate will revert to a permanent rate of 8.82 percent. Prior to the Enacted Budget, the rate was due to decrease to 6.85 percent on January 1, 2025. The knowledge that the top rate will remain at the elevated level may induce a larger number of affected taxpayers to leave the State.

In addition, a large share of taxpayers upon whom the higher rates are imposed are nonresidents of New York. Of taxpayers with taxable incomes over $1 million, over one-half are nonresidents, with the share rising from 52.7 percent in 2015 to 54.4 percent in 2019. While these taxpayers still provide revenue for the State, the tax is only imposed upon the income that is sourced in New York; on average, that is less than one-quarter of their total income.

[7] Estimated based on tax year 2019 personal income tax data.

With the new tax rates, nonresidents would potentially be paying nearly $2.9 billion in New York personal income taxes. However, should these taxpayers decide to move this income out of New York, it will have a large impact on the State's revenues.

Currently, there is a case before the Supreme Court, *New Hampshire v. Massachusetts*, relating to the taxation of income earned by nonresidents working from home during the pandemic which could have implications for New York.[8] For example, if ten percent of nonresidents' income is no longer sourced in New York, PIT collections could decline by over $285 million annually.

[8] The lawsuit claims that the imposition of the Massachusetts personal income tax on income earned by New Hampshire employees of Massachusetts' businesses who worked remotely during the pandemic is unconstitutional.

IV. Recommendations

Continue to Bolster Reserve Funds

The Financial Plan anticipates deposits to rainy day fund reserves will bring the new total to $3.3 billion – significantly lower than the $6.4 billion that is statutorily authorized, and lower than is likely necessary to weather future revenue shortfalls caused by economic downturns or unexpected circumstances. At $3.3 billion, the available reserve funds would equal only 3.7 percent of forecasted General Fund disbursements for SFY 2021-22, or less than 14 days of average daily disbursements.

The SFY 2020-21 financial management strategy employed during the COVID-19 economic crisis exemplifies the inadequacy of the State's current reserve fund levels. Rather than using available reserves, the State deferred up to 20 percent of certain local assistance payments to not-for-profit service providers and local governments for temporary savings. Although withheld funds were mostly repaid as the financial situation improved, the tactic created significant hardship to service providers and local governments facing their own fiscal emergencies.

Through the first two months of SFY 2021-22, total State tax receipts exceeded the Financial Plan forecast by $4 billion. To the extent that collections remain above forecast and are not needed to cover unanticipated expenses, these unanticipated revenues should be used to further bolster the rainy day fund reserves. For future years, this Office has proposed a method to grow the State's reserve funds to a more appropriate total of 10 percent of General Fund reserves.[9] The State should commit to strengthening reserves so that critical spending obligations can be met even in times of crisis or when prior year commitments come due.

Use Federal Aid Prudently and Transparently

The Enacted Budget Financial Plan is presented as balanced through the end of SFY 2022-23, thanks largely to the use of federal recovery aid. Federal enabling legislation, regulations and guidance permit fairly flexible use of these funds by states and local educational agencies.

These principles should guide the use of federal recovery aid:

1. *Spread the use of federal funding out over the life of the Financial Plan.* Policymakers should maintain the currently planned multi-year utilization of these funds, which reduces imbalance between spending commitments and available revenues over the life of the Financial Plan and limits the risk of a "funding cliff" for critical programs when federal assistance ends.

2. *Avoid using federal funding to support recurring spending.* While fiscal relief aid received under ARP can be used to make up for revenue shortfalls, the State should not create

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

new programs or make long-term spending commitments that are initially funded by federal aid; this will only increase pressure on State finances in later years. The Financial Plan indicates the State prudently plans to use much of its federal aid to provide temporary and necessary assistance to struggling New Yorkers and businesses; to the extent the recovery gains momentum and these programs are successful, their need will wind down with the funding available.

3. *Clearly identify details of planned expenditures and ensure transparent and timely reporting of the use of the funds.* The Enacted Budget includes an extraordinary amount of federal aid, as well as appropriation language for recovery initiatives that grants broad discretion to the Executive in designing program terms and conditions. Given the importance of these funds to the economic and fiscal recovery of the State, a high level of public disclosure – both in detail and timeliness – regarding the intended uses and progress administering these funds should be provided by the Executive.

Closely Monitor Personal Income Tax Receipts and Taxpayer Behavior

The Enacted Budget will increase New York's reliance on high-income earners by setting the highest PIT rate in permanent law at 8.82 percent and establishing a temporary top rate of 10.9 percent through 2027. The combination of this high reliance, volatility of capital gains, and the possibility of taxpayer migration in reaction to the high new rates creates a risk for the Financial Plan that should be carefully monitored to ensure appropriate and timely responses to any shortfalls in PIT receipts are developed.

Restore Prudent Debt Policies

When adopting the SFY 2020-21 budget, policymakers faced a growing public health emergency, a deepening fiscal crisis, uncertainty regarding the ability to access capital markets, and potential cash flow shortages that could compromise critical State operations. In that context, authorization to use extraordinary debt management techniques – including cash flow borrowing and suspension of the debt limitations imposed by the Debt Reform Act – was reasonable.

However, when the SFY 2021-22 budget was adopted, these emergency circumstances had largely abated, yet the Enacted Budget extended the emergency debt powers. The result is the existing statutory debt limitations have become functionally meaningless. The State's debt issuance expectations are unsustainable within the debt limit, and debt service costs are expected to increase from $6.4 billion to $8.8 billion over the Financial Plan period.

With the State financial condition stabilized, policymakers should restore prudent debt policies, including the establishment of updated and binding limits on State debt. In addition, policymakers should replace some planned debt issuances with more "pay-as-you-go" funding to reduce long-term debt service obligations, including limiting debt uses to capital projects related to State assets. In the near term, if State tax receipts continue to surpass forecasts, a portion of the additional revenue could be used for this purpose. The State should also work to reduce the scope of the overall capital program by prioritizing investments on critical asset maintenance and development.

Appendices

Appendix A

Summary of Receipts and Disbursements
SFY 2020-21 through SFY 2024-25
General Fund
(in millions of dollars)

	SFY 2020-21 Actual	SFY 2021-22 Enacted Budget	Percentage Growth	SFY 2022-23 Projected	SFY 2023-24 Projected	SFY 2024-25 Projected	Average Annual Growth Out-years
Receipts:							
Taxes Including Transfers from Debt Service Funds							
Personal Income Tax	44,034	53,275	21.0%	59,708	62,300	65,038	6.9%
Consumption and Use Taxes	11,766	15,394	30.8%	15,177	15,533	15,805	0.9%
Business Taxes	6,420	6,986	8.8%	7,660	7,492	6,945	-0.2%
Other Taxes	2,332	2,124	-8.9%	2,253	2,372	2,493	5.5%
Total Taxes	*64,552*	*77,779*	*20.5%*	*84,798*	*87,697*	*90,281*	*5.1%*
Miscellaneous Receipts	7,515	1,775	-76.4%	1,750	1,794	1,858	1.5%
All Other Transfers From Other Funds	2,245	7,630	239.9%	4,707	4,487	6,030	-7.5%
Total Receipts	**74,312**	**87,184**	**17.3%**	**91,255**	**93,978**	**98,169**	**4.0%**
General Fund Disbursements							
Local Assistance Grants							
Economic Development and Government Oversight	122	974	699.2%	125	125	125	-49.6%
Parks and Environment	1	9	1046.7%	2	2	2	-38.5%
Transportation	107	123	15.1%	115	115	115	-2.1%
DOH Medicaid inc. Administration	13,871	15,864	14.4%	19,325	20,237	20,953	9.7%
Other Health	841	711	-15.5%	655	661	666	-2.1%
Social Welfare	3,081	5,390	75.0%	3,231	3,352	3,359	-14.6%
Mental Hygiene	1,910	4,515	136.4%	4,285	4,182	4,457	-0.4%
Public Protection/Criminal Justice	118	271	130.6%	146	146	146	-18.7%
Higher Education	3,313	2,943	-11.2%	3,035	3,103	3,173	2.5%
School Aid	23,046	24,673	7.1%	26,718	29,659	31,405	8.4%
Other Education	1,930	2,595	34.5%	2,558	2,644	2,755	2.0%
General Government	65	136	107.8%	123	123	123	-3.2%
Local Government Assistance	666	768	15.4%	795	795	795	1.2%
Other	(88)	2,069	-2454.2%	1,823	2,270	2,376	4.7%
Total Local Assistance Grants	*48,981*	*61,041*	*24.6%*	*62,936*	*67,414*	*70,450*	*4.9%*
Departmental Operations							
Personal Service	7,154	9,835	37.5%	9,386	9,527	9,558	-0.9%
Non-Personal Service	2,950	2,553	-13.5%	2,962	3,044	3,266	8.6%
Total Departmental Operations	*10,104*	*12,388*	*22.6%*	*12,348*	*12,571*	*12,824*	*1.2%*
General State Charges	7,032	8,435	20.0%	8,984	9,545	10,728	8.3%
Debt Service	326	392	20.2%	400	458	506	8.9%
Capital Projects	4,540	3,863	-14.9%	3,982	3,665	3,576	-2.5%
Other Transfers To Other Funds	3,112	2,872	-7.7%	2,903	2,597	2,616	-3.1%
Total Disbursements	**74,095**	**88,991**	**20.1%**	**91,553**	**96,250**	**100,700**	**4.2%**

Appendix B

Summary of Receipts and Disbursements
SFY 2020-21 through SFY 2024-25
State Operating Funds
(in millions of dollars)

	SFY 2020-21 Actual	SFY 2021-22 Enacted Budget	Percentage Growth	SFY 2022-23 Projected	SFY 2023-24 Projected	SFY 2024-25 Projected	Average Annual Growth Out-years
Receipts:							
Taxes							
Personal Income Tax	54,967	61,050	11.1%	65,494	68,448	71,348	5.3%
Consumption and Use Taxes	15,596	17,548	12.5%	18,475	18,931	19,411	3.4%
Business Taxes	8,256	9,000	9.0%	9,853	9,690	9,045	0.2%
Other Taxes	2,381	2,169	-8.9%	2,291	2,406	2,530	5.3%
Total Taxes	*81,200*	*89,767*	10.6%	*96,113*	*99,475*	102,334	4.5%
Miscellaneous Receipts	25,109	17,031	-32.2%	16,939	16,599	16,824	-0.4%
Federal Grants	61	429	603.3%	275	50	45	-52.8%
Total Receipts	**106,370**	**107,227**	**0.8%**	**113,327**	**116,124**	**119,203**	**3.6%**
Disbursements:							
Local Assistance Grants							
Economic Development and Government Oversight	171	1,435	739.6%	436	237	251	-44.1%
Parks and Environment	5	12	127.8%	6	6	6	-22.5%
Transportation	3,648	3,792	3.9%	4,194	4,196	4,196	3.4%
DOH Medicaid inc. Admin	19,346	21,631	11.8%	24,509	25,517	26,338	6.8%
Other Health	1,812	1,905	5.1%	2,384	2,385	2,402	8.0%
Social Welfare	3,081	5,395	75.1%	3,236	3,357	3,363	-14.6%
Mental Hygiene	1,913	4,521	136.3%	4,292	4,197	4,479	-0.3%
Public Protection/Criminal Justice	300	702	133.8%	576	592	592	-5.6%
Higher Education	3,313	2,943	-11.2%	3,035	3,103	3,173	2.5%
School Aid	26,706	28,164	5.5%	30,963	33,790	35,576	8.1%
Other Education	3,968	4,588	15.6%	4,422	4,401	4,405	-1.3%
General Government	230	474	105.8%	342	355	360	-8.8%
Local Government Assistance	666	768	15.4%	795	795	795	1.2%
Other	(72)	404	-658.1%	190	188	185	-23.0%
Total Local Assistance Grants	*65,087*	*76,734*	17.9%	*79,378*	*83,118*	*86,120*	3.9%
Departmental Operations							
Personal Services	12,355	14,453	17.0%	14,220	14,324	14,409	-0.1%
Non-Personal Service	5,651	4,808	-14.9%	5,381	5,399	5,647	5.5%
Total Departmental Operations	*18,006*	*19,261*	7.0%	*19,601*	*19,723*	*20,056*	1.4%
General State Charges	7,918	9,518	20.2%	10,098	10,673	11,870	7.6%
Debt Service	13,196	6,707	-49.2%	5,863	6,440	6,878	0.8%
Capital	-	-	0.0%	-	-	-	0.0%
Total Disbursements	**104,207**	**112,221**	**7.7%**	**114,940**	**119,955**	**124,924**	**3.6%**

Appendix C

Summary of Receipts and Disbursements
SFY 2020-21 through SFY 2024-25
All Funds
(in millions of dollars)

	SFY 2020-21 Actual	SFY 2021-22 Enacted Budget	Percentage Growth	SFY 2022-23 Projected	SFY 2023-24 Projected	SFY 2024-25 Projected	Average Annual Growth Out-years
Receipts:							
Taxes							
Personal Income Tax	54,967	61,050	11.1%	65,494	68,448	71,348	5.3%
Consumption and Use Taxes	16,117	18,154	12.6%	19,089	19,549	20,032	3.3%
Business Taxes	8,792	9,601	9.2%	10,471	10,308	9,661	0.2%
Other Taxes	2,500	2,288	-8.5%	2,410	2,525	2,649	5.0%
Total Taxes	*82,376*	*91,093*	*10.6%*	*97,464*	*100,830*	*103,690*	*4.4%*
Miscellaneous Receipts	30,772	26,052	-15.3%	26,598	26,314	25,958	-0.1%
Federal Grants	78,152	96,645	23.7%	76,322	71,721	70,054	-10.2%
Total Receipts	**191,300**	**213,790**	**11.8%**	**200,384**	**198,865**	**199,702**	**-2.2%**
Disbursements:							
Local Assistance Grants							
Economic Development and Governm	920	2,240	143.6%	1,500	1,487	1,183	-19.2%
Parks and Environment	215	324	50.3%	472	472	472	13.4%
Transportation	6,289	6,819	8.4%	6,811	6,467	6,464	-1.8%
DOH Medicaid inc. Administration	65,325	68,576	5.0%	73,243	73,364	75,020	3.0%
Other Health	7,680	10,446	36.0%	5,727	5,573	5,636	-18.6%
Social Welfare	11,963	14,988	25.3%	10,794	9,362	8,477	-17.3%
Mental Hygiene	2,136	4,878	128.3%	4,702	4,526	4,806	-0.5%
Public Protection/Criminal Justice	2,323	4,478	92.8%	3,126	1,743	1,742	-27.0%
Higher Education	3,323	2,955	-11.1%	3,049	3,117	3,180	2.5%
School Aid	29,043	34,934	20.3%	38,909	40,635	40,425	5.0%
Other Education	4,747	5,611	18.2%	5,451	5,389	5,316	-1.8%
General Government	312	557	78.3%	477	466	508	-3.0%
Local Government Assistance	666	1,181	77.3%	1,208	795	795	-12.3%
Other	(171)	1,000	-685.8%	(650)	(646)	(441)	-176.1%
Total Local Assistance Grants	*134,771*	*158,986*	*18.0%*	*154,817*	*152,751*	*153,582*	*-1.1%*
Departmental Operations							
Personal Service	14,793	15,281	3.3%	14,906	15,012	15,094	-0.4%
Non-Personal Service	7,375	9,269	25.7%	7,391	7,311	7,071	-8.6%
Total Departmental Operations	*22,168*	*24,550*	*10.7%*	*22,297*	*22,323*	*22,165*	*-3.3%*
General State Charges	9,260	9,973	7.7%	10,474	11,050	12,247	7.1%
Debt Service	13,298	6,749	-49.2%	5,863	6,440	6,878	0.6%
Capital Projects	7,090	8,629	21.7%	9,818	10,163	9,741	4.1%
Total Disbursements	**186,587**	**208,887**	**12.0%**	**203,269**	**202,727**	**204,613**	**-0.7%**

Appendix D

Summary of Receipts and Disbursements
SFY 2020-21 through SFY 2024-25
Federal Funds
(in millions of dollars)

	SFY 2020-21 Actual	SFY 2021-22 Enacted Budget	Percentage Growth	SFY 2022-23 Projected	SFY 2023-24 Projected	SFY 2024-25 Projected	Average Annual Growth Out-years
Receipts:							
Special Revenue Funds	76,124	93,891	23.3%	74,037	69,467	67,814	-10.3%
Debt Service Funds	74	72	-2.7%	70	67	62	-4.9%
Capital Funds	1,954	2,682	37.3%	2,215	2,187	2,178	-6.7%
Total Receipts	**78,152**	**96,645**	**23.7%**	**76,322**	**71,721**	**70,054**	**-10.2%**
Disbursements:							
Local Assistance Grants							
Economic Development Government Oversight	8	9	12.0%	9	9	9	-0.9%
Parks and Environment	3	1	-60.6%	1	1	1	-0.8%
Transportation	64	101	56.1%	61	61	61	-15.6%
DOH Medicaid inc. Administration	44,739	46,945	4.9%	48,733	47,847	48,682	1.2%
Other Health	6,642	7,971	20.0%	2,488	2,489	2,505	-32.0%
Social Welfare	8,263	8,521	3.1%	6,384	5,037	4,562	-18.8%
Mental Hygiene	166	211	27.2%	252	186	186	-4.1%
Public Protection/Criminal Justice	1,975	3,717	88.2%	2,517	1,117	1,117	-33.0%
Higher Education	(0)	-	-100.0%	-	-	-	0.0%
School Aid	2,269	6,570	189.6%	7,526	6,425	4,499	-11.9%
Other Education	735	941	28.1%	940	939	882	-2.1%
General Government	74	58	-21.1%	8,525	7,422	5,439	353.8%
Local Assistance Grants	-	413	100.0%	413	-	-	-100.0%
Other	(495)	(468)	-5.4%	(468)	(468)	(468)	0.0%
Total Local Assistance Grants	*64,444*	*74,990*	*16.4%*	*77,380*	*71,065*	*67,477*	*-3.5%*
Departmental Operations							
Personal Service	2,438	828	-66.0%	686	688	685	-6.1%
Non-Personal Service	1,724	4,461	158.8%	2,010	1,912	1,424	-31.7%
Total Departmental Operations	*4,162*	*5,289*	*27.1%*	*2,696*	*2,600*	*2,109*	*-26.4%*
General State Charges	1,342	455	-66.1%	376	377	377	-6.1%
Debt Service	72	70	-2.8%	67	62	62	-4.0%
Capital Projects	1,097	1,588	44.8%	1,127	1,119	1,069	-12.4%
Total Disbursements	**71,045**	**82,322**	**15.9%**	**81,579**	**75,161**	**71,032**	**-4.8%**

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