

New York City Residents May Be Asked To Pay a Little More in Taxes

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On January 1 New York City welcomed its 109th mayor: Bill de Blasio (D). This edition of Noonan's Notes previews the new mayor's tax agenda, with a focus on his plan to increase the personal income tax rate on the city's highest-income earners in order to fund education. De Blasio must now convince Albany politicians to grant the state's largest city the freedom to advance his plan.

On January 1, New York City welcomed a new mayor. And it may cost the city's wealthiest residents their daily Starbucks lattes.

Two months after winning a landslide victory in the race to become the 109th mayor of New York, Bill de Blasio (D) walked onto the steps of City Hall and delivered his inaugural address, reiterating his campaign promise to "take dead aim at the Tale of Two Cities."¹ Included in his progressive proclamation,² the mayor stressed one of his central campaign promises to raise the personal income tax rate on the city's highest-income earners in order to pay for universal pre-kindergarten. While his early-education initiative is his signature objective involving city taxes, de Blasio has used his time so far as mayor to hint at other tax-related goals. This column previews the changes that may be on the horizon as Gracie Mansion welcomes its newest resident.

For practitioners with clients in New York City, de Blasio's tax-related goals can't come as welcome news — at least to their clients. City taxpayers already pay state and local

income taxes at likely the highest rates in the nation. Indeed, this is what fuels many of the residency audits covered so often in this column.

The Mayor Pledges to Move Forward With a Tax Increase

A who's who list of New York politicians — Michael Bloomberg, Bill Clinton, Hillary Clinton, Gov. Andrew Cuomo (D), and U.S. Sen. Charles Schumer, D-N.Y. — sat shoulder to shoulder as de Blasio delivered his inaugural address. The address covered a wide range of issues, from paid sick leave, to affordable housing, to stop-and-frisk, to, as is most relevant to this column, taxes.

Addressing his campaign promise to fund early-education initiatives through a tax increase, de Blasio reiterated that his administration will "ask the very wealthy to pay a little more in taxes so that we can offer full-day universal pre-K and after-school programs for every middle school student." Of course, the mayor won't be "asking" residents to pay higher taxes; "demanding" may be the more appropriate word. Whatever the case, without boring his audience with the full details of his plan (don't worry, we do that below), the mayor noted that "when we say 'a little more,' we can rightly emphasize the 'little.'" According to de Blasio, those earning between \$500,000 and \$1 million would see their taxes increase by an average of \$973 a year. "That's less than three bucks a day — about the cost of a small soy latte at your local Starbucks," quipped the mayor. Of course, higher earners would be out a little bit more than a cup of coffee; the mayor's proposal would serve as a pretty significant tax hike for the city's wealthiest residents.³

That New York City's progressive champion would reiterate his campaign promise to raise taxes is not surprising, but for those interested in city finances (or in Starbucks

³Because the tax applies only to the amount of taxable income that exceeds \$500,000, New York City residents with taxable income of \$750,000 would see their annual city income taxes increase by \$1,335. Taxpayers with taxable income of \$2 million, however, would see their taxes increase by \$8,010, and taxpayers with taxable income of \$10 million would see their taxes increase by more than \$50,000 — significantly more than the daily cost of a Starbucks latte. See de Blasio, "Starting Early, Learning Longer: Education Investments to Keep NYC Competitive," Public Advocate for the City of New York.

¹See Inaugural Address of Mayor Bill de Blasio, New York City.

²The mayor used the word "progressive" no less than six times in his address.

beverages), it's worth taking a deeper look at what the plan proposes and what its chances are of coming to fruition.

Tax to Fund Education Investment Plan

The mayor's plan to raise taxes is part of a comprehensive strategy to expand early learning opportunities for New York City schoolchildren. The plan, first announced while de Blasio served as the city's public advocate, seeks to provide all 4-year-olds with access to universal pre-K, closing a gap of nearly 50,000 children who, according to the mayor, currently receive either no pre-K or inadequate part-time pre-K.⁴ Also, the plan calls for an expansion of after-school programs for middle school students. The programs are to be financed through city grants to local schools that would allow schools to partner with community-based organizations to implement after-school learning opportunities.⁵

According to de Blasio's campaign plan entitled "A New Path Forward: A Long-Term Plan to Tackle Economic Inequality and Improve Income Mobility," the mayor seeks to fund these initiatives by increasing the city's income tax on wealthy residents earning more than \$500,000 from 3.876 percent to 4.41 percent.⁶ The tax applies only to the amount of a taxpayer's income that exceeds \$500,000, and according to the mayor, this five-year surcharge will yield \$530 million in new revenue to pay for universal pre-K and to fund after-school programs.⁷

Although a constant theme in the mayor's inaugural address was that change will happen quickly, de Blasio recognized that his "progressive vision isn't universally shared." And while he vowed to overcome the obstacles impeding his movement toward "one city," when it comes to taxes, de Blasio failed to mention the one critical hurdle he must face: Albany.

Cities Are Creatures of the State

The idea that cities are creatures of the state, and therefore subject to their authority, is based on what is known as Dillon's Rule. The rule, which limits a municipal government's authority to act, derives from an 1868 decision by then-Iowa Supreme Court Justice John Dillon, barring a city the right to prevent the construction of a railroad through its streets.⁸ Dillon's Rule was then expanded on in Dillon's 1872 book, *A Treatise on the Law of Municipal*

Corporations, and it remains the legal doctrine governing city-state relationships throughout the United States today.

Although the doctrine is occasionally modified by individual state laws permitting home rule (whereby cities are given more autonomy), New York City's taxing authority remains, with few exceptions, subject to Dillon's Rule.⁹ Thus, most tax-related actions initiated (or trumpeted on the campaign trail) by the city (or by its popular mayor-elect) are subject to approval by the State Legislature and the governor.¹⁰ The question that logically follows from that check on the new mayor's authority is whether Albany will approve the proposed tax increase. While we have long since abandoned any claim to a Delphian insight into the inner workings of the Legislature, there are a few factors to keep in mind.

First, Cuomo has been vocal of late regarding his intention to lower taxes — particularly the state's property and business taxes.¹¹ And the governor used his recent Executive Budget address to tackle the issue of universal pre-K head on: proposing statewide pre-K that's funded not with a tax increase but with the state's predicted budget surplus.¹² In addition to setting the stage for a political standoff with de Blasio (de Blasio quickly responded to the governor's budget address by reaffirming his plan to raise taxes), the governor's funding scheme suggests that Cuomo is hesitant about approving a tax increase on voters he wants to win over in his bid for reelection by promising lower taxes. Speaking of reelection, both the governor and members of the Legislature, including the Republican-controlled State Senate, face an election in 2014, which raises the question whether now is the right time for Albany politicians to approve a tax increase on residents of the state's largest city.

Voters, however, seem to overwhelmingly support de Blasio's early education initiative and its source of funding. The mayor won his seat by the widest margin for a non-incumbent in city history, and according to a Quinnipiac

⁹N.Y. Const. Art. XVI, section 1. See also, *Expedia, Inc. v. City of New York Dept. of Finance*, No. 180, 2013 N.Y. slip op 7759 (N.Y. Nov. 21, 2013) (finding that a New York state enabling statute authorized New York City to impose a hotel room occupancy tax on payments to hotel remarketers who acted as intermediaries between hotels and guests) ("In New York, local governments lack an independent power to tax. The State Constitution vests the taxing power in the State Legislature and authorizes the Legislature to delegate that power to local governments.") (internal citations omitted).

¹⁰See, e.g., N.Y. Tax Law section 1301 (authorizing New York City to impose a tax on the personal income of city residents); N.Y. Tax Law section 1304 (mandating the rates for the city personal income tax).

¹¹See "Governor Cuomo Announces Plan to Provide More Than \$2 Billion in Tax Relief to New York's Families and Businesses" (Jan. 6, 2014). The governor had previously appointed two commissions to render suggestions to further his tax-reduction goals. See New York State Tax Relief Commission Final Report (Dec. 2013).

¹²See 2014-15 Executive Budget (Jan. 21, 2014).

⁴*Id.*

⁵*Id.*

⁶Bill de Blasio, "A New Path Forward: A Long-Term Plan to Tackle Economic Inequality and Improve Income Mobility," Bill de Blasio for Mayor. New York City's highest rate tax bracket was set at 3.876 percent for residents with taxable incomes more than \$500,000 for tax years beginning after 2009. TSB-M-10(7)I.

⁷*Id.*

⁸*Clinton v. Cedar Rapids and Miss. River R. R. Co.*, 24 Iowa 455 (1868).

University poll, 63 percent of state voters support the mayor's tax plan.¹³ That popular support may sway Albany politicians on the campaign trail, and at least one member of the Legislature has put forth a bill that would let the city increase its individual income tax rate by 0.75 percent to a new top level of 4.63 percent.¹⁴ While only time will tell whether de Blasio's initiative will become law, it is worth noting that the mayor would not be the first city executive to convince Albany of a need to temporarily raise income tax rates. Between 2003 and 2005, the city raised income tax rates on those making more than \$150,000 to 4.46 percent. That higher rate was also in place from 1991 to 1998 to pay for the "Safe Streets, Safe City" initiative.

Few will fault the mayor's objective to improve early education opportunities, but while Albany decides whether to support the mayor's plan, critics question the policy implications of earmarking a tax increase. The city's wealthiest residents may worry that if Albany does not put the brakes on de Blasio's agenda, what will stop the city from going back to the well each time it faces an unfunded agenda item and taking more than just a soy latte from the city's high-income earners.

Tax Objectives Beyond Early Education — Empty Expenditures and Empty Lots

While his tax agenda largely focuses on the proposed rate increase on the city's wealthiest residents, de Blasio has offered other hints as to policy objectives that tax professionals (and taxpayers) will want to keep an eye on.

First, de Blasio has pledged to replace corporate tax giveaways with a new economic development focus. According to the mayor, "New York City currently disperses around \$4 billion a year on economic development, including \$3 billion on tax expenditures that too often go to single large companies. Yet many of those projects would have happened even in the absence of the tax and subsidy giveaways."¹⁵ In response, de Blasio has proposed reforms of all tax breaks — and elimination of programs with "notoriously weak payoffs," like the Industrial and Commercial Abatement Program (ICAP), which provides property tax abatements for eligible industrial and commercial buildings that are built, modernized, rehabilitated, expanded, or otherwise physically improved.¹⁶ While broad in nature, the purpose of that objective appears to be to ensure that tax

expenditures create real jobs and that funds that could be used for citywide development are not lost to ineffective tax breaks.

Second, the new mayor has placed considerable emphasis on increasing the supply of affordable housing throughout the city. While encouraging development is often furthered with various tax incentives, de Blasio appears to favor the stick over the carrot. As part of his plan to unlock vacant properties and direct new revenue to affordable housing, de Blasio is seeking to close what he perceives is a tax loophole and change how vacant lots are taxed.¹⁷ Vacant lots that are zoned residential — regardless of their development potential — are currently lumped into the same property category as single-family homes.¹⁸ That means that those vacant lots are assessed at 6 percent of their market value, whereas multi-unit residential and commercial properties are assessed at 45 percent of their market value. The mayor hopes to unlock the vacant land by applying the same tax rate to large vacant lots as to commercial properties — that is, increase the assessment value on the vacant lots to 45 percent of their market value.¹⁹ The idea is that this tax increase (or, as proponents argue, loophole closure) will encourage development by punishing real estate speculators who idly sit on valuable swathes of land that could, instead, provide space to increase housing stock throughout the city. The additional tax revenue that will result from the land left idle would be earmarked for a city affordable housing fund.²⁰ As with his early education initiative, however, supporters of this proposal will have to wait and see if the mayor can persuade Albany to adopt his plan.

If Dillon wasn't already the bane of New York City progressives' existence (hint: he wasn't), he may soon well be.

Conclusion

Mayor de Blasio, the first Democrat to win the office in two decades, rode a wave of progressive support to City Hall. He campaigned as the voice of the disenfranchised and promised to address the city's spreading inequalities. Much of the city (and the state) appears convinced, largely because those who view themselves as victims of inequality are no longer just the tired, the poor, and the huddled masses, but rather middle-income residents who feel forgotten in their city. Whether tax increases are the answer remains to be seen. But what is clear is that Albany will likely have to step aside if de Blasio wants to test his theory. ☆

¹³"New York State Voters Back De Blasio Tax Plan 2-1," Quinipiac University (Nov. 27, 2013).

¹⁴S 6011, 2013 Reg. Sess. (N.Y. 2013).

¹⁵See de Blasio, "Jobs for All New Yorkers, Growth for All Neighborhoods," Bill de Blasio for Mayor.

¹⁶N.Y.C. Adm. Code section 11-269.

¹⁷See de Blasio, "Safe, Affordable Homes for All New Yorkers," Bill de Blasio for Mayor.

¹⁸N.Y. Real Prop. Tax Law section 1802.

¹⁹See de Blasio, "Foundation for an Affordable City: An 8-Point Plan to Increase and Protect Affordable Housing Across New York City," Public Advocate for the City of New York.

²⁰See *supra* note 17.