

The Economic Impact of Losing the Full Deductibility of State and Local Taxes in New York State

Rockefeller Institute of Government
New York State Division of the Budget

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Rockefeller
Institute of Government



Division of the Budget

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The following analysis of the cap on the deductibility of the state and local taxes (SALT) implemented by the Federal Tax Cuts and Jobs Act of 2017 (TCJA) was conducted before New York State became the epicenter of the Coronavirus Disease 2019 (COVID-19) pandemic and nationwide efforts to stop the spread of the virus led to the shutdowns of large segments of the New York economy. In the context of the pandemic, the conclusions drawn by this report are more urgent than ever.

New York State's opposition to the SALT cap – and that of similarly situated states – is well documented. The SALT cap marked a departure from more than 100 years of U.S. tax law with the implementation of the first double tax in our nation's history. It puts these states at a competitive disadvantage, assaulting our economies and undermining the decisions made by our voters to make investments in health care, education, and infrastructure. New York, in particular, is already the nation's largest donor state, sending \$29 billion more annually to Washington than it gets back in return. The SALT cap exacerbates this imbalance.

These very same states hardest hit by the SALT cap are also the hardest hit by the pandemic. As a result of New York's population density and its role as a port of entry for Europeans visiting the U.S. who brought the virus with them, the state has had exponentially more deaths caused by COVID-19 than any other state in the nation.

Even as New York is the epicenter of the public health crisis, it is still not getting a fair share of federal funding. In just one example, the federal government methodology for delivering emergency funding to hospitals doesn't recognize the crisis and is directing about \$12,000 per COVID-19 case to hospitals in New York State while other states are receiving about \$300,000 per case, according to Kaiser Health. Federal action thus far will result in states with a fraction of the impact measured in confirmed cases, deaths, or economic impact receiving proportionally more funding than New York State.

The ongoing implementation of the SALT cap is compounding this inequity and will ultimately slow the ability of the New York State economy -- and the nation's with it -- to recover when businesses are re-opened. As the following report concludes, if the SALT cap were eliminated, New York State's economy would support an average of 107,000 more full-time jobs annually and return billions of dollars to the State's GDP.

In New York, our disciplined approach to state finances has made it possible for the state to make strides in strengthening our economic foundation since the last recession. We are leading the nation with a \$275 billion investment in infrastructure and have lowered income tax rates for every New Yorker. The pandemic is already weakening the state's ability to continue these investments going forward, sapping the state of more than \$13 billion in revenue. The SALT cap creates additional head winds that we simply cannot afford and in the absence of federal support to offset these revenue losses, deep cuts in state spending that will further impede economic growth must be made.

Simply put, the SALT cap raised taxes on over one million New Yorkers and is an obstacle to recovery. The federal government must rescind the SALT cap and unleash the full power of the New York State economy to effectuate a full recovery of the national economy. The evidence is clear in the analysis that follows.

Sincerely,

A handwritten signature in blue ink, appearing to read "R. Mujica, Jr.", written in a cursive style.

Robert F. Mujica, Jr.
Director of the Budget

Foreword

The Federal Tax Cut and Jobs Act of 2017 made significant changes to the individual and corporate income tax, including the loss of full deductibility of state and local taxes. Now capped, taxpayers from across New York were almost immediately affected by the limitation on the deduction available for state and local taxes (SALT). The provision increased the tax burden, which, in turn, had negative impacts as spending in the New York economy slowed.

The Rockefeller Institute of Government and the New York State Division of the Budget have examined the impact of the SALT cap. This report shows that the cap, which is effectively a tax increase for New Yorkers, is having a sustained negative effect on employment and output in New York State. New York supports 107,000 fewer additional jobs annually with the greatest losses in New York City and the surrounding metro area. Each \$1 in additional tax burden lowers New York's economic output by \$1.17. The effects are felt by workers in the services, construction, retail, and wholesale trade sectors.

The report also highlights the unequal distribution of the SALT cap burden across the states. New York along with New Jersey, Massachusetts, and Connecticut are among the most negatively affected states. The Institute's annual report "Giving or Getting? New York's Balance of Payments" shows that these states subsidize federal spending and have the largest negative balance of payments (the amount of federal revenues received minus the amount paid in taxes). The SALT cap only exacerbates this deficit.

It is important to note that the US and New York are entering a period of economic uncertainty. Over the past two months, New York has become the national epicenter for the COVID-19 epidemic and the efforts to stop the spread of the virus have led to a near complete shutdown of the US economy. The magnitude and duration of the impact of the COVID-19 pandemic on the New York economy is yet to be determined.

The analysis presented in this report was completed before the pandemic. The conclusions, here, may need to be scaled as we better understand the impact of the crisis on New York. The Institute will continue to work with the Division of the Budget to understand how New York's economy, fiscal health, and balance of payments are affected by the crisis.

Sincerely,

A handwritten signature in black ink, appearing to read 'Patricia Strach', with a stylized flourish extending to the right.

Patricia Strach
Interim Executive Director
Rockefeller Institute of Government



The Economic Impact of Losing the Full Deductibility of State and Local Taxes in New York State

Executive Summary

The Federal Tax Cut and Jobs Act (TCJA),¹ signed into law on December 22, 2017, made significant changes to the individual and corporate income tax. The act is frequently compared to Federal reforms that were enacted in 1986 as a comprehensive tax reform package. Unlike the 1986 reforms, changes to the individual income tax have drawn the most attention in New York and many other high-income states. Specifically, the 2017 law eliminates the full deductibility of state and local taxes by capping deductions. This provision was used to finance other tax reductions in the TCJA. The state and local tax (SALT) reductions further shifted the already disproportionate burden of Federal revenue generated in high-income states.

The Rockefeller Institute of Government and the New York State Division of the Budget (DOB) have examined the impact of the loss of the full value of the Federal itemized deduction for state and local taxes. Beginning in calendar year 2018, the deduction has been capped at \$10,000, resulting in a Federal tax increase that disproportionately impacts high-income taxpayers; these taxpayers account for a significant portion of New York's annual personal income tax liability.

The purpose of this study is to analyze the economic effect of the state and local tax cap on New York in both the short- and long-term. We explore how the provisions of the TCJA impacted the economic and fiscal health of New York.

COVID-19

The following analysis of the cap on the deductibility of the state and local taxes (SALT) implemented by the Federal Tax Cuts and Jobs Act of 2017 (TCJA) was conducted before New York State was the epicenter of Coronavirus Disease 2019 (COVID-19) pandemic and nationwide efforts to stop the spread of the virus led to the shutdowns of large segments of the New York economy. The magnitude and duration of the impact of the COVID-19 pandemic on the New York economy is still to be determined.

Individual income tax revenue raised within New York will be lower than originally projected for this report. Still, the findings of this report can be scaled to address changes in tax burden. Each \$1 in additional tax burden caused by the SALT cap reduced total economic output in the state by \$1.17.

The Federal aid distributed in response to the COVID-19 crisis to date will also impact the Balance of Payments analysis.² For example, the Federal government methodology for delivering emergency funding to hospitals doesn't recognize the crisis and is directing about \$12,000 per COVID-19 case to hospitals in New York State while states such as Nebraska, Montana, and Minnesota are receiving about \$300,000 per case, according to Kaiser Health.³ Federal action to date will result in states with a fraction of the impact measured in confirmed cases, deaths, or economic impact receiving proportionally more funding than New York State.

The economic impact analysis in this report used two models to determine the effect of the SALT deduction as a distinct tax expenditure that was drastically reduced by the TCJA. We analyze the baseline impact of the new law by simulating the loss of household income available to spend in New York. First, we used the IMPLAN model to estimate the economic impact of one year to provide an economic baseline. Second, we supplemented the IMPLAN model with a REMI model, which was used to examine the impact of the elimination of the SALT deduction on several key economic indicators including employment, population, output, and housing prices. Results were compared to develop the estimates for lost economic activity in the short and long run to understand the economic impact.

The report uses tax estimates developed by the New York State Department of Taxation and Finance, which analyzed the impact of TCJA's various components on the state's tax code and estimated the fiscal impact of SALT on New York taxpayers. The department estimated that in one year, New York State households would pay an additional \$12.3 billion in personal income taxes and the SALT cap could cost taxpayers up to \$15 billion annually by 2025.⁴ This number represents the loss of economic activity in the state, effectively a tax increase, as these dollars are no longer available for households to spend in New York. This report examines the broader impacts of the increased tax burden on the New York economy.

Key findings are as follows:

- The enactment of the cap on the SALT deduction reduces income available to New Yorkers. Each \$1 reduction in personal income reduced total economic output in the state by \$1.17.
- If the 2017 SALT cap were eliminated, New York State's economy would support 107,000 additional full-time jobs annually, on average, in the first seven years (2018–24). Most of the additional jobs would have been created in New York City (55,000) and the greater New York City metro area (45,000) compared with the rest of the state (8,000).
- The employment losses are largest in the services, construction, and trade (wholesale and retail) sectors.
- New York's population would be 104,000 higher, on average, if the SALT cap were eliminated.
- Total economic activity lost as a result of the SALT cap ranges from \$14.4 billion to \$24.5 billion annually depending on the methodological approach used for analysis.
- Because housing prices and incomes are higher in New York City and the greater New York City metro area, these areas pay more in property and state income taxes, and take higher itemized deductions on their Federal taxes. As a result of the SALT cap, housing prices decline by 0.9 percent in New York City, 1.5 percent in the greater New York City metro area, and 0.2 percent in the rest of state on average in the first seven years.
- The states that are most affected by the limit of the SALT deduction are those that annually contribute more to the Federal budget than they receive in program expenditures (balance of payments).
- In 2018, New York ranked worst in the nation for its balance of payments, and bears the second largest increased burden as a result of the SALT deduction.

Introduction

The Tax Cuts and Jobs Act (TCJA) was signed into law on December 22, 2017.⁵ The law provided for substantial changes in the Federal individual income taxes, corporate income taxes, and other taxes with the policy goal of providing a stimulus for economic growth. Tax bases, rate modifications, and eliminations of certain deductions were enacted for both the individual and corporate taxes. The aggregate changes would provide total taxpayer relief estimated initially at \$1.5 trillion over the ten years. The revenue loss was revised in subsequent estimates to \$1.9 trillion.

The most significant changes to the individual income tax include the reduction in income tax rates, along with the expansion of the tax brackets. The standard deduction and child tax credit were increased and a new dependent tax credit was added. Modifications were made to the alternative minimum tax, and certain itemized deductions were limited. These changes took effect on January 1, 2018 and will expire after December 31, 2025.

The goals of the Federal changes were to provide tax relief for middle-income families, simplify the tax code for individuals, repatriate overseas income, and boost economic growth. Proponents at the time the TCJA was enacted believed that US economic growth would increase at a faster pace. The national level of full employment GDP, the output possible when the economy achieves its ideal level of employment, would expand. These expansions would be created by higher levels of investment in domestic capital stock encouraged by the TCJA. At the same time, several other macroeconomic shocks occurred, including rising trade tensions, elevated levels of economic policy uncertainty, four Federal Reserve rate hikes in 2018, three rate cuts in 2019, and a global economic slowdown especially on the manufacturing front. These have made it difficult for economists to quantify the macroeconomic impacts of the TCJA.

The macroeconomic impacts of TCJA continue to be debated nationally. The discussion includes both the effectiveness as a tax reform mechanism as well as the selective nature of the provisions. From the state perspective, however, the outstanding question remains: What is the impact on those states that already contribute more in terms of the Federal tax dollars than they receive in Federal spending? Simplification came with a cost as long-standing tax provisions were reexamined, amended, or eliminated. For example, SALT deductions have been historically distributed variably across states, with two large states characterized by high incomes and progressive tax structures—California and New York—jointly accounting for over one-third of nationwide SALT deductions. Table 1 shows how the distributions of SALT deductions claimed prior to the TCJA were highly concentrated in a few states.

TABLE 1. Pre-TCJA Distribution by State of the SALT Deduction, 2017

State	Average Adjusted Gross Income Per Return	State's Share of SALT Deductions
California	\$84,040	21.1%
New York	\$86,309	13.0%
New Jersey	\$88,599	5.7%
Texas	\$70,781	4.4%
Illinois	\$74,331	4.3%
Massachusetts	\$94,850	3.5%
Pennsylvania	\$68,446	3.4%
Florida	\$71,405	3.2%
Maryland	\$78,842	3.0%
Virginia	\$78,214	2.9%

SOURCE: Rockefeller Institute and New York State Division of Budget calculations based on IRS Statistics of Income, <https://www.irs.gov/statistics/soi-tax-stats-historic-table-2>.

Analysis of the efficacy of the SALT deduction as a distinct provision or as a part of a comprehensive reform have been the subject of numerous studies over the past 30 years. An analysis by Coen-Pirani and Sieg showed that:

Specifically, TCJA increases the relative tax burden of the most productive households that live in cities with high state and local taxes by about three percentage points. Historically, high-tax cities such as New York and San Francisco have been among the most productive cities in the US with the largest agglomeration externalities. The tax reform thus creates strong financial incentives for high-income households to leave these high-agglomeration cities.⁶

In New York, the personal income tax statute links to the Federal tax base and many definitional provisions. The TCJA resulted in an immediate flow through to New York's tax base and related state revenues were affected by many of these changes. To the extent flow-throughs had the potential to have a negative impact on New York taxpayers, the governor's State Fiscal Year (SFY) 2018-19 budget contained several provisions to correct for these changes. One of the key provisions of the Federal act relating to full value of their itemized deductions was corrected in New York by changes to the state statute that decoupled state and Federal deductions. This provision allowed a taxpayer to deduct the full cost of state and local real estate taxes paid that are over the \$10,000 Federal limit.⁷ Table 2 provides a summary of the key provisions of the act and New York's response.

TABLE 2. New York’s Response to TCJA

TJCA Provision	New York Response	Annual savings to Tax Payers (\$ millions)
Cap on SALT deductions	Decoupled	\$441
Restriction or repeal of numerous itemized deductions	Decoupled	\$269
Changes to standard deduction and personal exemption	Decoupled	\$840
Total annual savings		\$1,550

SOURCE: New York State Division of the Budget.

Although New York State has been able to mitigate some of the increased tax burden, it has not been able to fix it all. New York, along with New Jersey, Connecticut, and Maryland, filed a lawsuit in Federal court to overturn these changes to the Federal tax code.⁸

This report will assess the economic toll the loss of the full value of the Federal itemized deduction for state and local taxes has on New York State’s economy. We use economic modeling tools IMPLAN and REMI to estimate the impacts the SALT cap has had on New York’s key economic indicators. We then explore the current state of the relationship between New York and the Federal government through the framework of the balance of payments and show how it will be affected by the SALT cap deduction.

THE SIZE AND SCALE OF THE SALT DEDUCTION

In 2017, the last year of the full SALT deduction, 35 percent of all Federal income tax filers utilized the itemized deduction. Of these, 31 percent took the deduction for state and local taxes, with 25 percent deducting property taxes.⁹ In fiscal year 2018, the state and local deductions for state and local taxes and property taxes were among the largest tax expenditures, estimated to be worth more than \$110 billion.¹⁰

Economic Impact

The bulk of research estimating the impact of the TCJA, to date, has explored the cost effectiveness of the tax reforms. The consensus at the time was encouraging the expansion of the domestic capital stock would increase US economic growth at a faster pace and the level of real full employment (potential) GDP would be at a higher level. In April 2018, the Congressional Budget Office (CBO) initially estimated that the provisions would result in a reduction of \$65 billion in individual income taxes, \$94 billion in corporate taxes, and \$3 billion in other taxes. Total tax relief was estimated at \$163 billion in the first year (2018).¹¹

The initial CBO analysis and accompanying report indicated the recent tax cuts would “increase the supply of labor and capital in the economy thereby raising potential output throughout the project periods.”¹² Economic impact as a result of the TCJA has varied by forecaster, and, as the Congressional Research Service noted subsequent to enactment, “the data appear to indicate that not enough growth occurred in the first year to cause the tax cut to pay for itself.”¹³

Rather than looking at the relationship among different TCJA tax provisions (e.g. the higher standard deduction, increased child tax credit, and expanded tax brackets) this study examines the effect of the SALT deduction cap. The SALT deduction cap changed the income tax rates paid by New Yorkers. A number of studies examining the impact of income tax rates on locational decisions have found that taxes lower long-run employment levels in high-wage areas, leading to locational inefficiencies.¹⁴

A growing body of research examines the shift in total liability to high-income states that results from the SALT deduction cap. A Federal Reserve Bank of Atlanta study examined this shift and found:

the average percentage increase in remaining lifetime spending under the TCJA is 1.6 percent in red states versus 1.3 percent in blue states. Among the richest 10 percent of households, this differential is larger. Rich households in red states enjoyed a 2.0 percent increase compared to a 1.2 percent increase among the rich in blue-state households. This gap is driven almost entirely by the limitation on the SALT deduction. Excluding the SALT limitation from the TCJA results in a spending gain of 2.6 percent for rich red-state households compared to 2.7 percent for rich blue-state households.¹⁵

The New York State Department of Taxation and Finance analyzed the impact of TCJA’s various components on the state’s tax code and preliminary data from 2018 individual income tax filings. The department estimated a baseline annual impact on individual income tax burden of an additional \$12.3 billion. And, given the projections at the time the report was written, the SALT cap could cost taxpayers up to \$15 billion annually by 2025. This number represents a loss of economic activity in the state, effectively a tax increase, as these dollars are no longer available for households to spend in New York.¹⁶

The analysis completed for this report assumes the cap on the SALT deduction resulted in a \$12.3 billion higher personal income tax burden for New York tax filers in a baseline year. To examine the initial impact of the cap on the SALT deduction in New York State we calculated an estimate using two separate economic input-output models. The IMPLAN¹⁷ model was used for the initial baseline analysis. The REMI model was used to develop the potential long-term impacts. We compare the results of the two models.

Baseline Annual Impact—Utilization of the IMPLAN model

Our baseline analysis of the impact of TCJA used the IMPLAN model to examine the impact of the SALT cap over one year. IMPLAN is based on an input-output model that looks at the interdependencies between economic sectors. Input-output models can be used to estimate the impacts of a shock to an economy and analyze the resulting ripple effects. The impact of the SALT cap was modelled as a negative Household Income Change. According to analysis conducted by the New York State Department of Taxation and Finance, households in New York had \$12.3 billion less income to spend than if the SALT cap had not been enacted. The negative impact effects were distributed across three regions of New York as designated by the New York State Department of Taxation and Finance analysis: New York City, greater New York City metro area, and rest of the state.¹⁸ The bulk of the household income change was allocated to downstate, where the higher incomes and property values are concentrated.

IMPLAN Results

We calculated the first-year shock to New York as a result of the loss of the full value of SALT and found that each \$1 reduction in household income reduced economic output in the state by \$1.17. The baseline analysis shows \$5.4 billion less in labor income was available across the state because of the decreased funds available for spending and investment. These losses are primarily located in the downstate region, which accounts for 94 percent of the loss. The value-added generated in New York, the difference between output and the cost of intermediate inputs, fell by \$9.4 billion.

TABLE 3. Economic Impacts from Household Income Reduction, 2018: IMPLAN Analysis (\$ billions)

	Labor Income	Value Added	Output
New York City	(\$3.0)	(\$5.2)	(\$7.6)
Greater New York City Metro Area	(\$2.1)	(\$3.6)	(\$5.7)
Rest of State	(\$0.3)	(\$0.6)	(\$1.0)
Total	(\$5.4)	(\$9.4)	(\$14.4)

SOURCE: Rockefeller Institute of Government IMPLAN analysis of New York State Department of Taxation and Finance data.

TABLE 4. Output Impact by Industry, 2018: IMPLAN Analysis (\$ billions)

Description	New York City	Greater New York City Metro	Rest of State	Total	Share of Total Output Impact
Real estate	(\$0.95)	(\$0.69)	(\$0.07)	(\$1.71)	12%
Hospitals	(\$0.71)	(\$0.57)	(\$0.10)	(\$1.38)	10%
Owner-occupied dwellings	(\$0.59)	(\$0.49)	(\$0.08)	(\$1.16)	8%
Wholesale trade	(\$0.36)	(\$0.27)	(\$0.04)	(\$0.68)	5%
Insurance carriers	(\$0.24)	(\$0.17)	(\$0.04)	(\$0.44)	3%
Monetary authorities and depository credit intermediation	(\$0.17)	(\$0.14)	(\$0.03)	(\$0.35)	2%
Limited-service restaurants	(\$0.19)	(\$0.13)	(\$0.03)	(\$0.34)	2%
Offices of physicians	(\$0.16)	(\$0.14)	(\$0.02)	(\$0.32)	2%
Wired telecommunications carriers	(\$0.14)	(\$0.12)	(\$0.02)	(\$0.29)	2%
Junior colleges, colleges, universities, and professional schools	(\$0.19)	(\$0.07)	(\$0.02)	(\$0.28)	2%
Electric power transmission and distribution	(\$0.18)	(\$0.08)	(\$0.02)	(\$0.28)	2%
Other financial investment activities	(\$0.13)	(\$0.13)	(\$0.02)	(\$0.28)	2%
Full-service restaurants	(\$0.14)	(\$0.10)	(\$0.02)	(\$0.26)	2%
Retail - Nonstore retailers	(\$0.13)	(\$0.10)	(\$0.02)	(\$0.25)	2%
Legal services	(\$0.13)	(\$0.10)	(\$0.02)	(\$0.25)	2%
Nursing and community care facilities	(\$0.12)	(\$0.10)	(\$0.02)	(\$0.24)	2%
Wireless telecommunications carriers (except satellite)	(\$0.18)	(\$0.05)	(\$0.01)	(\$0.23)	2%
Retail - Food and beverage stores	(\$0.12)	(\$0.09)	(\$0.02)	(\$0.22)	2%
Retail - General merchandise stores	(\$0.08)	(\$0.08)	(\$0.02)	(\$0.17)	1%
Funds, trusts, and other financial vehicles	(\$0.08)	(\$0.06)	(\$0.01)	(\$0.15)	1%
Total	(\$7.63)	(\$5.74)	(\$0.99)	(\$14.36)	

SOURCE: Rockefeller Institute of Government IMPLAN analysis of Department of Taxation and Finance data.

The IMPLAN models allows for industry-level impact estimation. Table 4 shows the output impacts by industry. Overall, 65 percent of output losses are concentrated in 20 industries. The sectors most immediately affected were those where households have the highest levels of local spending: health care, dining, retail, and real estate. Households responded to the reduction in income caused by cutting back on medical care, dining out, and shopping. They also invested less in housing and real estate.

IMPLAN analysis allows for estimation of the short-term impacts on the SALT cap on New York's regional economies. It found that for every dollar a household lost in income due to the SALT cap in the first year, New York State economic output declined by \$1.17. As consumers had less available to spend, the health care, retail, dining, and real estate sectors were the most affected. The largest impacts were in New York City and surrounding metro region. The REMI PI model is designed to estimate the impact over the longer term.

Multi-Year Impact—Utilization of the REMI PI model

The New York State Division of the Budget's (DOB) multi-region REMI PI model was used to estimate the long-term impact of the SALT cap on New York's economy and its three regions: New York City, greater New York City region, and rest of the state.¹⁹ Two economic simulations were created in order to examine the SALT cap on the New York economy.

We assume that as of the first year of the SALT implementation, New York taxpayers realize \$12.3 billion less in disposable income due to the SALT deduction limitation. The departure from the REMI baseline starts in calendar year 2018 and ends in calendar year 2024. The simulation forecast horizon is 2018-24. For the REMI analysis and for years after 2018, the underlying SALT liability is increased based on the personal consumption price deflator.

Sensitivity Analysis Outline

Considering the analytical issues involved when other states' economies interact with New York's economy in the context of a nationwide SALT limit repeal, we implemented two scenarios to analyze the economic impact. These impacts were spread across the three regions according to their proportional concentration of SALT deduction claims by income class. As expected, most of the impact is felt downstate, in the New York City and greater New York City metro regions.

1. An upper bound scenario was first analyzed, where the *Personal Taxes* REMI variable was increased by \$12.3 billion. Therefore, we assume that an additional \$12.3 billion is taken out of the State's economy via the wage channel.
2. A lower bound scenario where the *Consumption Reallocation* variable, which measures the change in disposable income, was decreased by \$12.3 billion.

The lower bound scenario utilizes the consumption reallocation variable to dampen the overall economic impact in the REMI model by bypassing the relative compensation rate and affecting consumption through the marginal income effect on consumption. This has a more limiting impact on the economic simulation since economic migration and compensating disposable income differentials provide further dynamic linkages in the REMI modelling system. This type of scenario using the REMI system is somewhat like the traditional input-output models. The upper-bound scenario approach is more impactful than the lower-bound scenario approach since increasing personal income taxes has the effect of households and business leaving the state.

REMI Results

Upper Bound Scenario

The \$12.3 billion increase in *Personal Taxes* directly decreases the after-tax relative wage rate of the state, causing net out-migration in each region as workers move to where their after-tax wages are highest. The DOB REMI model does not explicitly incorporate interactions with other states. This is expected to magnify the effect of the SALT cap by failing to account for other neighboring states that would also see a decrease in their after-tax relative wage rates, thus dampening the out-migration from New York. In addition to net out-migration from the state, overall economic activity is dampened by a decrease in disposable income which drives less consumption in New York and, thus, overall economic activity and employment. Under this scenario, full-time equivalent employment in New York would be 136,000 lower on average for the next seven years due to the SALT cap. Population would be 156,000 lower.

Lower Bound Scenario

The Lower Bound Scenario was constructed to “compensate” for the Upper Bound Scenario, specifically by limiting the migratory response to an increase in after-tax relative wages. The \$12.3 billion reduction to *Consumption Reallocation* decreases household income available for saving and purchasing of consumer goods and services due to the SALT cap. Utilizing this variable, rather than the *Personal Taxes* policy variable, bypasses some of the linkages in REMI such as relative wages, net economic migration, and relative home prices and thus limits the overall economic impact. Under this scenario, full-time equivalent employment in New York would be 79,000 workers lower on average for the next seven years than had the SALT cap not occurred. Population would be only 53,000 lower.

Average of the Two Scenarios

To derive a point-estimate rather than a range between the two scenarios, the average of the results was used. Due to the SALT cap, New York State’s economy loses 107,000 more jobs annually on average in the first seven years; most of the job losses would occur in New York City (55,000) and the greater New York City metro area (45,000), compared with the rest of state (8,000). The employment losses were in the services, construction, and trade (wholesale and retail) sectors. Population would be 104,000 lower annually on average in the first seven years.

Because housing prices and incomes are higher in New York City and the greater New York City metro area, residents pay more in property and state income taxes, and, as a result, take higher itemized deductions in their Federal taxes. Thus, they fare the worst from the SALT cap. The analysis shows housing prices decrease by 0.9 percent in New York City, 1.5 percent in the greater New York City metro area, and only 0.2 percent in the rest of state on average in the first seven years.

Economic activity, as measured by real GDP lost by the SALT cap over the first seven years, is, on average, \$10.3 billion (2012 fixed \$). In terms of real output, \$16.3 billion (2012 fixed \$) is lost on annual average basis over the first seven years. Tables 5 and 6 provide a more detailed review of relevant economic variables for the state and by region.

TABLE 5. Economic Impacts on New York State: REMI-PI Analysis (2018-2024), Average of Upper and Lower Bound Scenarios, Differences from Baseline

Economic Variables	Five-Year Average	Seven-Year Average
Total Employment (thousands)	(110.9)	(107.2)
Private (thousands)	(104.0)	(99.9)
Population (thousands)	(90.3)	(104.3)
Net Economic Migrants (thousands)	(14.7)	(11.5)
Real Gross Domestic Product (2012 \$ billions)	(\$10.6)	(\$10.3)
Nominal Output (\$ billions)	(\$24.5)	(\$24.5)
Real Output (2012 \$ billions)	(\$16.7)	(\$16.3)
Personal Income (2012 \$ billions)	(\$9.9)	(\$10.4)
Disposable Personal Income (2012 \$ billions)	(\$14.6)	(\$15.2)
Real Disposable Income (2012 \$ billions)	(\$11.1)	(\$11.3)
Personal Consumption Expenditure—Price Index	(0.1)	(0.2)
Housing Price (percent deviation from baseline)		
New York City	(0.9%)	(0.9%)
Greater Metro Area	(1.5%)	(1.5%)
Rest of State	(0.2%)	(0.2%)
Employment by Sector (thousands)	Five-Year Average	Seven-Year Average
Total Employment	(110.9)	(107.2)
Natural Resources	(0.1)	(0.1)
Construction	(18.2)	(16.3)
Manufacturing	(1.9)	(1.8)
Retail and Wholesale	(18.2)	(17.7)
Transportation and Public Utilities	(3.2)	(3.0)
Finance, Insurance & Real Estate	(9.6)	(9.1)
Services	(52.8)	(51.8)
Government	(6.9)	(7.3)

NOTES: Greater New York City metro area includes Dutchess, Nassau, Orange, Putnam, Rockland, Suffolk, and Westchester counties. The departure from the REMI baseline starts in calendar year 2018 and ends in calendar year 2024. The simulation forecast horizon is 2018-24.

SOURCE: New York State Division of the Budget analysis.

TABLE 6. Economic Impacts by Region: REMI-PI Analysis (2018-24), Average of Upper and Lower Bound Scenarios, Differences from Baseline

	New York City	
	Five-Year Average	Seven-Year Average
Total Employment (thousands)	(56.5)	(54.7)
Population (thousands)	(43.1)	(49.7)
Personal Income (2012 \$ billions)	(\$4.9)	(\$5.1)
Disposable Personal Income (2012 \$ billions)	(\$7.5)	(\$7.7)
Real Gross Domestic Product (2012 \$ billions)	(\$6.0)	(\$5.8)
Real Output (2012 \$ billions)	(\$9.4)	(\$9.1)
Personal Consumption Expenditure—Price Index	(0.160)	(0.168)
	Greater New York City Metro Area	
	Five-Year Average	Seven-Year Average
Total Employment (thousands)	(46.1)	(44.5)
Population (thousands)	(41.2)	(47.6)
Personal Income (2012 \$ billions)	(\$4.5)	(\$4.8)
Disposable Personal Income (2012 \$ billions)	(\$6.3)	(\$6.5)
Real Gross Domestic Product (2012 \$ billions)	(\$3.9)	(\$3.8)
Real Output (2012 \$ billions)	(\$6.3)	(\$6.1)
Personal Consumption Expenditure—Price Index	(0.211)	(0.222)
	Rest of New York	
	Five-Year Average	Seven-Year Average
Total Employment (thousands)	(8.3)	(8.1)
Population (thousands)	(5.9)	(7.0)
Personal Income (2012 \$ billions)	(\$0.5)	(\$0.5)
Disposable Personal Income (2012 \$ billions)	(\$0.8)	(\$0.9)
Real Gross Domestic Product (2012 \$ billions)	(\$0.6)	(\$0.6)
Real Output (2012 \$ billions)	(\$1.1)	(\$1.0)
Personal Consumption Expenditure—Price Index	(0.046)	(0.048)

NOTES: Greater New York City metro area includes Dutchess, Nassau, Orange, Putnam, Rockland, Suffolk, and Westchester counties. The departure from the REMI baseline starts in calendar year 2018 and ends in calendar year 2024. The simulation forecast horizon is 2018-24.

SOURCE: New York State Division of the Budget analysis.

SALT Deduction Cap and the Balance of Payments

The SALT deduction cap exacerbates existing inequities among the states and Federal government through the balance of payments. The Rockefeller Institute annually develops an analysis to determine the Federal balance of payments. In its third year, the report provides an estimate of the distribution of Federal budget receipts and expenditures across the United States.²⁰ The analysis is intended to aid policymakers' understanding of redistribution and the impact of these decisions on the states. The most recent report estimates that in 2018, New York had the least favorable balance of payments of any state in the nation at -\$22.0 billion.

Certain states annually send more to the Federal government in revenue than they receive in spending. One of the goals of the Federal system is to provide for redistribution. However, the balance of payments analysis indicates that each year, New York and other high-income states, including New Jersey, Connecticut, and Massachusetts, consistently pay far more to the Federal government than they receive.

High-income earners will pay more under a progressive tax structure. States with more high-income earners, richer states, tend to pay more taxes per person to the Federal government and states with fewer high-income earners, poorer states, tend to receive larger payments per person, particularly for social programs

Historically, New York and other similarly situated states pay more in Federal taxes than they receive in Federal distribution, and TCJA has increased the disparity. Table 7 (next page) provides this comparison.

As Table 7 indicates, the states most affected by the SALT deduction limitation also contribute more to the Federal budget than they receive in program spending. The five states with the highest negative balance of payments in 2018 bear 32 percent of the SALT burden in 2019. The comparison shows that high-income states, which rely on a progressive tax structure to fund their government programs, have been penalized by TCJA for the fiscal choices they make.

The comparison of the excess burden generated by the SALT cap and the balance of payments shows that the Federal government has not reduced the fiscal burden on the states. The burden has been disproportionately worsened for the five of the higher-income states that already subsidize the Federal government. The SALT cap disfavored local income and property taxes, a key element of revenue generation in these states.

TABLE 7. Comparison of Balance of Payments and Impact of SALT

State	Balance of Payments, 2018 (\$ millions)	Balance of Payments Rank	SALT Burden, 2019 (\$ millions)	SALT Rank
New York	(21,986)	1	(14,661)	2
New Jersey	(11,518)	2	(5,639)	3
Massachusetts	(9,078)	3	(3,467)	4
Connecticut	(8,052)	4	(2,845)	6
Colorado	(1,557)	5	(1,060)	19
Minnesota	(725)	6	(1,893)	12
Utah	(511)	7	(426)	26
Nebraska	(315)	8	(325)	32
Illinois	344	9	(3,438)	5
New Hampshire	421	10	(205)	38
North Dakota	476	11	(70)	47
Wyoming	662	12	(41)	48
Washington	722	13	(410)	28
South Dakota	1,224	14	(28)	49
California	1,940	15	(23,392)	1
Vermont	2,160	16	(116)	46
Iowa	2,490	17	(429)	25
Nevada	2,762	18	(217)	37
Delaware	2,997	19	(145)	44
Rhode Island	3,129	20	(255)	35
Montana	4,188	21	(137)	45
Wisconsin	4,647	22	(1,391)	16
Idaho	5,523	23	(195)	39
Kansas	5,556	24	(343)	31
Alaska	6,570	25	(9)	50
Maine	6,940	26	(224)	36
Hawaii	8,210	27	(289)	34
Oregon	9,640	28	(1,151)	18
West Virginia	12,761	29	(146)	43
Arkansas	13,403	30	(376)	30
Texas	13,513	31	(1,242)	17
Indiana	14,595	32	(714)	22
Oklahoma	17,156	33	(414)	27
New Mexico	18,206	34	(149)	42
Mississippi	18,853	35	(166)	41
Georgia	20,025	36	(1,869)	13
Louisiana	20,288	37	(381)	29
South Carolina	23,044	38	(537)	23
Michigan	23,998	39	(1,415)	15
Florida	24,908	40	(2,024)	11
Missouri	25,009	41	(914)	20
Tennessee	25,306	42	(195)	40
Arizona	26,396	43	(769)	21
North Carolina	32,974	44	(1,716)	14
Pennsylvania	33,044	45	(2,579)	8
Ohio	34,641	46	(2,077)	10
Alabama	35,516	47	(308)	33
Kentucky	45,174	48	(510)	24
Maryland	47,937	49	(2,717)	7
Virginia	96,914	50	(2,324)	9

NOTES: The state-level SALT Tax Burden estimates were generated in 2018 by the Institute on Taxation and Economic Policy (ITEP) using a different methodology than the \$12.3 billion estimate produced by the Department of Taxation and Finance. The ITEP data are presented in the table to allow for state-level comparisons.

SOURCE: Rockefeller Institute of Government, *Giving or Getting? New York's Balance of Payments with the Federal Government*, <https://rockinst.org/wp-content/uploads/2020/01/1-22-20-Balance-of-Payments.pdf>; and Institute on Taxation and Economic Policy, *A Fair Way to Limit Tax Deductions*, 2018, <https://itep.org/a-fair-way-to-limit-tax-deductions/>.

The Future of the SALT Deduction

Fundamental reform of the current US tax structure offered the possibility of significant macroeconomic gains, but not without true sacrifice by certain groups. As we have seen in New York, specific taxpayers have seen their overall Federal tax liability increase as a result of the SALT cap. The additional burden affects these taxpayers as well as the economy as a whole. IMPLAN and REMI economic models indicate the scope of the effect in the short- and long-terms. Over a seven-year period, the SALT cap will annually suppress New York State GDP by \$10.3 billion and employment by 107,000 jobs. The largest impacts will be in the services, construction, and trade sectors.

On November 26, 2019, New York, Connecticut, Maryland, and New Jersey filed a notice of appeal to the US Court of Appeals for the Second Circuit to continue litigation against the Federal government for an unlawful and unprecedented cap on the deduction for state and local taxes. According to New York State Governor Andrew Cuomo: “The Trump administration’s SALT policy is retribution politics—plain and simple.” Further, “New York is already the nation’s leader in sending more tax dollars to Washington than we get back every year, and we will not allow this administration to pick the pockets of hard-working New Yorkers to fund tax cuts for corporations and send even more money to red states.”²¹

According to *Giving or Getting? New York’s Balance of Payments with the Federal Government*, the states which are actively seeking relief from the courts are those with a significantly distorted balance of payments.²² For the most recent four years, the states which have the largest negative balance include New York (\$116 billion), New Jersey (\$72 billion), Massachusetts (\$47 billion), and Connecticut (\$35 billion). These states are also most negatively affected by the SALT deduction.

The interaction of the Federal system of taxation and that of the states are related to each other. The recent action by the Federal government has not reduced the fiscal burden on states; if anything, as enacted, the changes dramatically increase that burden.

Endnotes

- 1 Federal Tax Cuts and Jobs Act of 2017, Public Law 115-97, 131 Stat. 2054, US Government Publishing Office, December 2017, <https://www.govinfo.gov/content/pkg/PLAW-115publ97/pdf/PLAW-115publ97.pdf> (accessed March 25, 2020).
- 2 Laura Schultz and Michelle Cummings, *Giving or Getting? New York's Balance of Payments with the Federal Government* (Albany: Rockefeller Institute of Government, January 2020), <https://rockinst.org/wp-content/uploads/2020/01/1-22-20-Balance-of-Payments.pdf>.
- 3 Jay Hancock et al., "Furor Erupts: Billions Going To Hospitals Based On Medicare Billings, Not COVID-19," *Kaiser Foundation*, April 10, 2020, <https://khn.org/news/furor-erupts-billions-going-to-hospitals-based-on-medicare-billings-not-covid-19/>.
- 4 The \$12.3 billion estimate of tax burden presented in this report was calculated by the New York State Department of Tax and Finance. The baseline estimate is based on a preliminary analysis of 2018 returns adjusted for the income shifted out of 2018 in response to the SALT limitation. The value is preliminary and revised estimates would yield different economic impact results. For example, the COVID-19 crisis means that actual tax revenue from 2020 on is likely to differ from estimates here and the impact estimates would need to be scaled accordingly.
- 5 Federal Tax Cuts and Jobs Act of 2017, Public Law 115-97, 131 Stat. 2054.
- 6 Daniele Coen-Pirani and Holger Sieg, "The impact of the Tax Cut and Jobs Act on the spatial distribution of high productivity households and economic welfare," *Journal of Monetary Economics* 105 (2019): 45.
- 7 For additional information regarding these changes, see "New York State Decouples from Certain Personal Income Tax Internal Revenue Code (IRC) Changes for 2018 and After," TSB-M 18-(6)I Income Tax, New York State Department of Taxation, December 28, 2018, <https://www.tax.ny.gov/pdf/memos/income/m18-6i.pdf>.
- 8 Office of New York Governor Andrew M. Cuomo, "Governor Cuomo and Attorney General James Announce Filing of Appeal in Multi-State Lawsuit Against Trump Administration's SALT Reform," press release, November 26, 2019, <https://www.governor.ny.gov/news/governor-cuomo-and-attorney-general-james-announce-filing-appeal-multi-state-lawsuit-against>.
- 9 "Individual Income Tax Returns with Exemptions and Itemized Deductions," SOI Tax Stats—Individual Statistical Tables by Size of Adjusted Gross Income, US Internal Revenue Service, accessed March 25, 2020, https://www.irs.gov/statistics/soi-tax-stats-individual-statistical-tables-by-size-of-adjusted-gross-income#_grp2.
- 10 "Table 3: Income Tax Expenditures Ranked by Total Fiscal Year 2018-2027 Projected Revenue Effect," *Tax Expenditures—Fiscal Year 2019* (Washington, DC: US Department of Treasury, Office of Tax Analysis, October 16, 2017): 34, <https://www.treasury.gov/resource-center/tax-policy/Documents/Tax-Expenditures-FY2019.pdf>.
- 11 *The Budget and Economic Outlook: 2018 to 2028* (Washington, DC: US Congressional Budget Office, April 2018), <https://www.cbo.gov/system/files/2019-04/53651-outlook-2.pdf>.
- 12 *Ibid.*, 7.
- 13 Jane Gravelle and Donald Marples, *The Economic Effects of the 2017 Tax Revision: Preliminary Observations* (Washington DC: Congressional Research Service, May 22, 2019), <https://fas.org/sgp/crs/misc/R45736.pdf>.
- 14 David Albouy, "The Unequal Geographic Burden of Federal Taxation," *Journal of Political Economy* 117, 4 (August 2009): 635-67.
- 15 David Altig, et al., "Did the 2017 Tax Reform Discriminate against Blue State Voters?," Federal Reserve Bank of Atlanta Working Paper Series 2019-7 (April 2019), 1, <https://eml.berkeley.edu/~auerbach/07-did-the-2017-tax-reform-discriminate-against-blue-state-voters-2019-04-10.pdf>.
- 16 The \$12.3 billion estimate of tax burden presented in this report was calculated by the New York State Department of Tax and Finance. The baseline estimate is based on a preliminary analysis of 2018 returns adjusted for the income shifted out of 2018 in response to the SALT limitation. The value is preliminary and revised estimates would yield different economic impact results. For example, the COVID-19 crisis means that actual tax revenue from 2020 on is likely to differ from estimates here and the impact estimates would need to be scaled accordingly.
- 17 IMPLAN is a regional economic analysis software application that is designed to estimate the impact or ripple effect (specifically backward linkages) of a given economic activity within a specific geographic area through the implementation of its Input-Output model.

- 18 Greater New York City metro area includes Dutchess, Nassau, Orange, Putnam, Rockland, Suffolk, and Westchester counties.
- 19 Three regions are defined as New York City, Greater New York City Metro Area (Nassau, Suffolk, Dutchess, Orange, Putnam, Rockland, and Westchester counties), and Rest of State.
- 20 Schultz and Cummings, *Giving or Getting?*.
- 21 Office of New York Governor Andrew M. Cuomo, "Governor Cuomo and Attorney General James Announce Filing of Appeal in Multi-State Lawsuit Against Trump Administration's SALT Reform."
- 22 Schultz and Cummings, *Giving or Getting?*, 13-14.



CONTRIBUTIONS

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