

**Joint Fiscal Committee Budget Hearing
Testimony
On Taxes and Economic Development Policy in
the
2008-2009 Executive Budget Proposal**

**Provided by
Ron Deutsch, Executive Director
New Yorkers for Fiscal Fairness**

February 11, 2008

I would like to thank the distinguished members of the Senate and Assembly fiscal committees for the opportunity to speak here today. My name is Ron Deutsch and I am the Executive Director of New Yorkers for Fiscal Fairness (NYFF). NYFF is a statewide non-profit organization focused on promoting fair taxation for all NYS residents within the context of the state budget process.

A Better Choice for “One New York”

To grow New York’s economy we must invest in New York’s working families. A healthy state economy requires well-educated New Yorkers, safe communities, affordable health care, affordable housing and a sound transportation infrastructure.

In recent decades, state budget policies have placed increasing pressure on local property taxes and local sales taxes. And the state government then came to the rescue with a program that provides rebate checks to all homeowners, regardless of need, and not enough to those who are truly overburdened by the increases in local taxes.

The Governor and the Legislature must work together to ensure that the 2008-09 state budget is fair to New York’s families by balancing the state budget in an equitable manner that makes the state tax system fairer and begins to actually reduce the pressure on the local property and sales tax bases rather than shifting more of the tax burden onto the backs of low and middle income New Yorkers.

We can promote tax fairness, strengthen local economies and help struggling families by:

Creating a Tax System that is FAIR to all New Yorkers: The wealthiest New Yorkers’ pay a much smaller percentage of their incomes in state and local taxes than low and middle income working families. Seniors on fixed incomes, working families and young couples are among the New Yorkers who suffer from the inequities in the current state-local tax structure. New York’s policymakers must take the pressure off the property tax by restoring some of the income tax system’s lost progressivity and closing corporate tax loopholes that allow some of the nation’s largest corporations to avoid paying their fair share of taxes.

Strengthening Local Communities: Rather than putting increased pressure on the local property and sales tax bases and then providing “relief” to local taxpayers in the form of state rebate checks, New York State policymakers must work together to reduce the pressure on local property and sales tax bases by restoring the state’s commitment to “revenue sharing” with its local governments and having the state government take over a greater share of local education and healthcare costs. And the state’s STAR programs must be targeted to provide adequate relief to those families that are most in need.

It’s time for New York State to end the special treatment of the favored few by:

Closing loopholes that allow large, profitable corporations to avoid paying their fair share of state taxes.

Stopping sweetheart deals with high-priced consultants who are being overpaid to do jobs that state workers can do better and cheaper.

Lowering drug prices for state and local governments by using New York’s purchasing power to get a fair deal from the drug companies.

Reforming economic development programs by improving the effectiveness and accountability of Industrial Development Agencies (IDAs), the Brownfield Clean Up Program (BCP) and the Empire Zones program.

Enacting the Bigger, Better Bottle Bill and making the beverage bottling industry return unclaimed bottle deposits.

Making New York's tax system fairer and more equitable by increasing the top marginal tax rates on the highest income households.

TAXES

Governor Spitzer has recently created a Property Tax Commission to examine the root causes of high property taxes in NYS. It is undeniable that property taxes have been increasing dramatically over the last two decades. We must acknowledge however, that property tax increases are not occurring in a vacuum but rather have a direct relationship to many tax and non-tax variables.

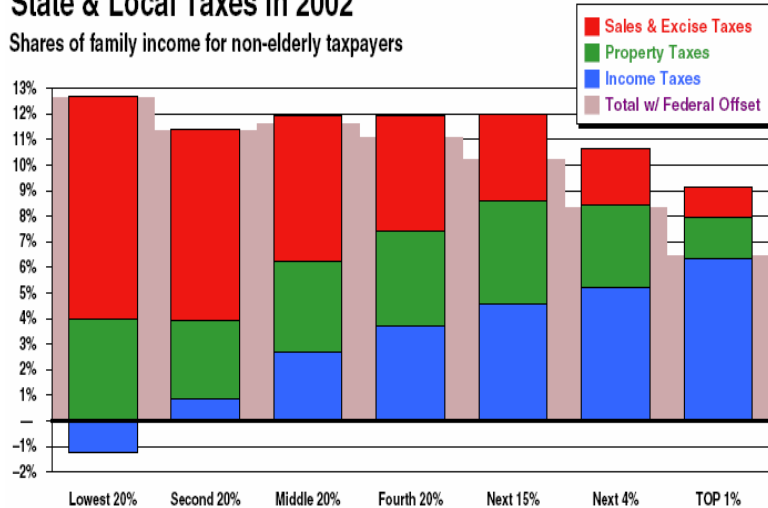
The Pataki tax cuts of 1994, now fully phased in, have resulted in NYS collecting \$16 billion less in revenue on an annualized basis that it would have had we not enacted these tax cuts. New York State has also reneged on its revenue sharing commitments with municipalities across the state, providing them with far less funding that they should receive under Section 54 of the State’s General Municipal Law.

The State has also, over a period of time reduced the overall percentage it pays as a portion of education aid, leaving local tax payers to make up the difference.

New York

State & Local Taxes in 2002

Shares of family income for non-elderly taxpayers



Income Group	Lowest 20%	Second 20%	Middle 20%	Fourth 20%	Top 20%		
					Next 15%	Next 4%	TOP 1%
Income Range	Less than \$15,000	\$15,000 – \$27,000	\$27,000 – \$44,000	\$44,000 – \$74,000	\$74,000 – \$160,000	\$160,000 – \$634,000	\$634,000 or more
Average Income in Group	\$8,700	\$20,700	\$34,900	\$56,800	\$102,000	\$250,000	\$1,663,000
Sales & Excise Taxes	9.5%	7.5%	5.7%	4.5%	3.4%	2.2%	1.2%
General Sales—Individuals	3.9%	3.6%	2.9%	2.5%	1.9%	1.3%	0.7%
Other Sales & Excise—Ind.	2.7%	1.6%	1.1%	0.7%	0.5%	0.3%	0.1%
Sales & Excise on Business	2.9%	2.3%	1.7%	1.3%	0.9%	0.6%	0.4%
Property Taxes	4.4%	3.0%	3.5%	3.7%	4.1%	3.2%	1.6%
Property Taxes on Families	3.9%	2.7%	3.1%	3.2%	3.5%	2.7%	0.7%
Other Property Taxes	0.5%	0.4%	0.4%	0.5%	0.5%	0.6%	0.9%
Income Taxes	-1.2%	0.8%	2.7%	3.7%	4.6%	5.2%	6.3%
Personal Income Tax	-1.3%	0.8%	2.6%	3.7%	4.5%	5.1%	6.0%
Corporate Income Tax	0.0%	0.0%	0.1%	0.0%	0.0%	0.1%	0.3%
TOTAL TAXES	12.7%	11.4%	11.9%	11.9%	12.0%	10.6%	9.1%
Federal Deduction Offset	-0.0%	-0.1%	-0.3%	-0.8%	-1.8%	-2.3%	-2.7%
TOTAL AFTER OFFSET	12.6%	11.3%	11.6%	11.1%	10.2%	8.4%	6.5%

Note: Table shows 2002 tax law at 2000 income levels.

Low and middle-income families in New York pay a far higher share of their income in state and local taxes than the richest New Yorkers. The richest 1% - those with an average income of \$1.6 million – pay only 9.1% of their income in state and local taxes; after the federal offset, the effective tax rate is only 6.5%. The tax rate on families in the middle-of-the-income distribution (\$27,000 and \$44,000) is 11.9%; 11.6% after the federal offset. The poorest New Yorkers – those below \$15,000 – pay at the highest tax rate, 12.6%. (see chart)

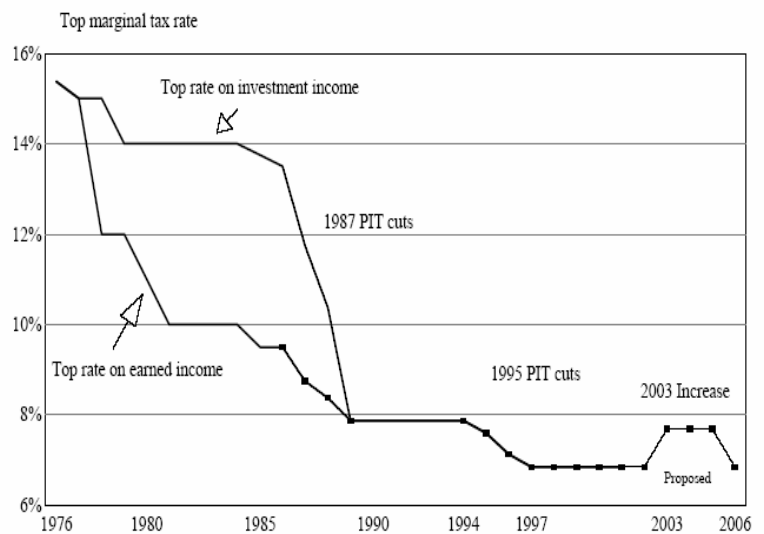
Since the state began reducing the top marginal rate on the personal income tax (PIT), tax regressivity has actually increased. Approximately 40% of the PIT cuts went to the top 5% of New York wage earners. While the introduction of a state earned income tax credit has helped, much of that benefit has been eaten up by increased sales and property taxes.

Overall, state and local taxes average 12.0% of income (2nd highest nationally), compared to a national average of 10.10% (Maine is highest at 13.0% ((Source: Tax Foundation)). New York has particularly high property taxes, which negatively impact low and middle income families, since they spend a high percentage of their income on housing. However, in recent decades New York has primarily cut the personal income tax instead, which mainly impacts higher income households.

New York has substantially reduced its top personal income tax rates over the last two and a half decades. New York State's top personal income tax rate was 15.375% in the early and mid-1970s. At that time, New York had the 3rd highest income tax rate of all the states with income taxes. The current rate of 6.85% places New York 14th among the 42 states with personal income taxes.

It is also important to realize that the states with which New York has the most direct economic competition, Connecticut and New Jersey, have moved in the opposite direction. New Jersey's top rate is now 8.97%, more than three and a half times higher than its mid-1970s rate and, since 1991, Connecticut has had a broad-based personal income tax, the top rate of which was increased from 4.5% to 5% in 2003.

New York State has cut its top personal income tax rate by more than 50% over the last 25 years.



NYS should focus on shifting the burden from the property tax (regressive) to the income tax (progressive). This can be done by increasing the top marginal rates on the wealthiest wage earners. It is unfair that someone making \$45,000 pays the same tax rate as someone making \$4.5 million.

STAR Rebates/Circuit Breaker Bill:

The Governor has delayed the proposed 17 % increase in STAR rebates in his Budget Proposal. I believe that the STAR rebate checks are not the best way to deliver property tax relief since it is not as targeted as it should be. A check for a few hundred dollars is little comfort to someone with a property tax bill over \$5,000.

We should instead be linking property tax relief to income in a more targeted fashion. One proposal that is currently gaining some support in the legislature is for a Property Tax Circuit Breaker.

It is important to acknowledge that the Middle Class STAR rebate program is better targeted than the original STAR exemption program in that it takes income into consideration. But it is still not adequately targeted to be an effective and efficient property tax relief mechanism since it does not take the size of a homeowner's property tax bill into consideration and it is still based on county and school district average of important variables.

A circuit breaker like the one proposed by Assemblywoman Sandra Galef and Senator Elizabeth Little (A.1575/S.1053) would address these shortcomings. A.1575/S.1053 applies to homeowners who have lived in their current homes for at least 10 years and who have incomes of below \$200,000. The credit under this proposal is 70% of the amount by which a household's property taxes on its primary, owner-occupied residence exceeds 6% of their income if their income is below \$100,000; 7% of their income if their income is between \$100,000 and \$150,000; or 8% of their income if their income is between \$150,000 and \$200,000.

The Fiscal Policy Institute estimated that in 2006 there about 1.9 million households that met the basic criteria (i.e., incomes of \$200,000 or less and 10 years at the same location), and that of those households, about seven hundred thousand would qualify for about \$1.23 billion of tax credits.

Corporate Taxes

The share of total state taxes contributed by the corporate income tax has steadily declined from 10.5% in 1979 to 7.6% in 1989 to 6.5% in 2000. We are now slightly above the national average of 6.3%. The state has added so many loopholes to our corporate tax program that New York City, which has rejected many of the loopholes, now collects more corporate income tax than the State (\$2.817 billion vs. \$2.258 billion in 2001-02). (Citizens for Tax Justice)

Some of the largest companies doing business in NYS are paying little or nothing in state corporate income taxes. The corporate loopholes that exist at both the federal and state level have resulted in some large corporations actually having a negative tax liability. According to a report from the Institute on Taxation and Economic Policy (2005) the many major companies, despite record profits, paid little or nothing in state corporate taxes between 2001-2003.

Last year the state passed a version of Combined Reporting which will help make sure that the large corporation doing business in NYS pay their fair share of taxes.

NYFF supports the Governor's efforts to continue to close corporate tax loopholes and we specifically support the following loophole closures as well:

The following reforms will generate over \$434 million on an All Funds Basis in previously uncollected State tax revenue:

Amend Definition of Gain from Sales of Real Property for Nonresidents. This Budget would close a loophole that allows nonresidents to place a property located in New York State in a partnership or LLC for the purpose of avoiding paying personal income tax when their ownership interest is sold. This measure will generate \$10 million annually starting in 2009-10.

Definition of "Presence in New York" for Residents Usually Outside the Country. This Budget proposes to close a loophole by amending the definition of "presence in New York" for determining residency of taxpayers who usually reside outside the country. The spouses and children of these taxpayers would only need to be present in New York for 90 days to be subject to State taxes, not necessarily present at the taxpayers' permanent place of abode in New York. This measure will generate \$5 million in revenue annually starting in 2009-10.

Tax Shelter Reporting. This Budget would provide the Department of Taxation and Finance with permanent statutory tools to address the increasing use of abusive tax shelters. Tools, which were originally scheduled to sunset July 1, 2009, but would be made permanent, include:

Requiring the disclosure of information related to transactions that present the potential for tax abuse;

Authorizing New York to promulgate regulations that would require the reporting of New York taxable transactions;

Providing substantial penalties for nondisclosure and the underpayment of taxes; and

Extending the statute of limitations for assessments relating to these transactions.

This measure will generate \$17 million annually starting in 2009-10.

REITs and RICs Reform. This Budget would make statutory corrections and structural alterations necessary to eliminate remaining tax loopholes with respect to real estate investment trusts (REITs) and regulated investment companies (RICs). It would require all captive REITs and captive RICs to file a combined return with the closest corporation that directly or indirectly owns or controls the captive. These amendments address the loopholes that remain despite legislation enacted in 2007. These amendments also simplify the approach to controlled REITs and RICs. This measure will generate no additional revenue, but is necessary to preserve revenue anticipated from the 2007 legislation.

Require Non-Profit Tax-Exempt Organizations to Collect Sales Tax On Certain Sales, Rentals and Leases. This Budget would close a current loophole that allows non-profit entities to compete on an unfair basis with other vendors, requiring them to collect tax on activities not directly related to their non-profit status. This measure will generate \$7.5 million in 2008-09 and \$15 million when fully effective.

Curtail Certain Tax Avoidance Schemes. This Budget proposes to narrow both the sales tax exemption for commercial aircrafts and the use tax exemption for motor vehicle, vessel,

and aircraft. This will help curtail certain abusive sales and use tax avoidance schemes. This measure will generate \$4 million in 2008-09 and \$6.3 million when fully effective.

Qualified Production Activities Income (QPAI) Decoupling. Conforming New York's tax code to the practices of 18 other states, this Budget proposes to decouple the State from the Federal deduction related to qualified production activities, requiring taxpayers to add back this deduction for State tax purposes.

The deduction was originally intended to provide a tax incentive to manufacturers by preserving and promoting domestic production and manufacturing jobs. However, the deduction is now allowed on a vast array of activities that go beyond the familiar concept of manufacturing. A multi-state firm currently could use the deduction to reduce its New York taxes without having a single production employee in the State. This method of tax avoidance will no longer be available. This measure will generate \$56 million annually starting in 2008-09.

Classify Credit Card Companies Doing Significant Business in New York as Taxpayers Under the Bank Tax. This Budget would subject out-of-State credit card companies to New York taxation on the revenue they collect from New York merchants and consumers ("economic nexus"). This measure will generate \$95 million in 2008-09 and \$75 million when fully effective.

Brownfields Tax Credit Reform. This Budget would refocus State environmental clean-up efforts by expanding potential remediation credits and providing meaningful caps to redevelopment credits available under the Brownfields Program. This measure is revenue neutral during the five-year financial plan period, but will produce significant savings in the years following.

Empire Zone Reform. The Empire State Development Corporation will administratively decertify existing Empire Zone businesses that failed to meet certain performance targets, and enforce more stringent qualification standards for new Empire Zone businesses. These changes are expected to generate \$50 million in savings annually starting in 2008-09.

Merge Fuel Taxes into One Petroleum Business Tax. This Budget recommends combining the petroleum business tax, the motor fuel tax and the State sales tax on motor fuel and diesel motor fuel into one petroleum business tax. This will offer greater transparency and simplify tax forms, making the tax easier to administer. This proposal would increase revenues by \$13.2 million in 2008-09 and \$55.9 million when fully effective.

Capital Base Rate Reduction and Cap Elimination. This Budget would reduce the corporation franchise tax capital base rate, eliminate the tax liability cap on this base for non-manufacturers, and conform the definition of "manufacturer" under the capital base to the definition under the entire net income base.

The tax rate would be reduced from 0.178 percent to 0.15 percent. The conforming amendments would specifically exclude electricity generation from the definition of manufacturing.

This bill would provide further tax relief to corporations with capital base liability below \$1 million doing business in New York State and increase the liability of those who previously benefited from the \$1 million cap. This measure will generate \$98 million in 2008-09 and \$70 million when fully effective. Small businesses that qualify for the reduced rates will receive tax relief totaling \$42 million annually.

Restructure Fees and Minimum Taxes Imposed on Limited Liability Companies (LLCs) and Corporations. This Budget proposes to restructure LLC fees and corporate minimum taxes to impose a similar fee on all partnerships and S corporations. Under the new structure, LLC fees would be based on a measure of New York activity (income) rather than the total number of members in a LLC. This measure will generate \$75 million annually starting in 2008-09.

Reclassify Certain Beverages. The tax treatment of certain flavored malt beverage products would be changed to better reflect alcohol content. These products will be taxed at the low liquor rate rather than the beer rate. This measure will generate \$15 million in 2008-09 and \$18 million when fully effective.

Redefine Little Cigars. Little cigars, which are indistinguishable from cigarettes, would be classified as cigarettes for tax and stamping purposes by both the State and New York City, and made subject to the requirements of the Master Settlement Agreement. This measure will generate \$3.6 million in 2008-09 and \$4.8 million when fully effective.

Study Tax Policy Toward Non-residents. The Department of Taxation and Finance would be directed to conduct a study of current taxation policies on non-residents with a limited work presence in New York. This will be done administratively.

“Amazon Tax.” Establish an evidentiary presumption that certain sellers using New York residents to solicit sales in the State are “vendors” required to collect sales and use tax. For example, many internet retailers enter into agreements with organizations under which the organization receives a commission if it includes a link on its website that connects users to the internet retailer’s website. If the customer makes a purchase, the organization receives a commission from the retailer. When the resident engages in solicitation activities in the State, such as distributing advertising fliers or newsletters in order to refer potential customers to the seller and maximize his or her commission income, the resident is acting as a “representative” and the seller is acting as a “vendor.” Enactment of this bill is necessary to implement the 2008-2009 Executive Budget because it would increase revenues by \$43 million in 2008-09 and \$73 million in 2009-10.

Economic Development

Empire Zones:

The state’s “leading” economic development program is broken. The Comptroller found in 2004 that more than two-thirds of the company’s seeking tax breaks failed to meet their job creation promises and that 23 % actually cut jobs.

Making the Empire Zones live up to their promise of revitalizing depressed areas will require *action in Albany* and every year that passes without reform is another year of wasted resources. Empire Zones can still have a role in helping New York improve its economy, the depressed regions and additionally protect the environment from additional suburban sprawl.

The Spitzer Administration recently released Emergency Regulations that would change the operation of the Empire Zone Program. I support many of the following changes to the program including:

- Regionally Significant Projects must export a substantial portion of goods/services out of State.
- Timeframe for job creation is reduced from 5 years to 3 years.
- Raise benefit-cost ratio from 15:1 to 20:1 and create floor of 5:1 for projects justified using non-quantifiable factors.
- Tighten the definitions of strategic industries and supply chain companies for a firm claiming supply-chain status as a non-quantifiable factor in its benefit-cost calculation.

NYFF also supports reforming the program further by adopting the following changes to the program on a permanent basis and having them codified into law:

Making Empire Zones More Accountable

- Implementing full, annual disclosure of the benefits received and the jobs provided by each participating business (The Syracuse Post-Standard recently won a law suit allowing for the release of some of this data). This information should further be posted on the internet to allow for greater transparency.
- Strengthening rather than weakening the program's focus on the state's neediest areas by prohibiting zone designations in areas other than census tracts that meet economic hardship criteria and immediately adjoining census tracts in the same community. Similarly, the extension of existing zones boundaries into areas other than census tracts meeting economic hardship criteria should be eliminated.
- Requiring the Commissioners of Labor and Economic Development to hold well-advertised and timely public hearings on all proposed business certifications, all contested de-certifications and all proposed boundary amendments. (Note: Hearings on boundary amendments are currently required but the Commissioner of Economic Development views this requirement as being met by the hearings held by local legislative bodies on the local laws making those boundary amendments. Public hearings are not currently required on business certifications and decertifications.)
- Requiring that all of the tax breaks and other benefits available to participating firms be based on the number and quality of the jobs actually created. (NOTE: Some but not all of the program's benefits are currently tied to the number of jobs actually created.)
- Strengthening the program's job quality standards and the application of these standards to all zone benefits. (NOTE: Under current law employers are eligible for an enhanced wage credit [\$3,000 as opposed to the ordinary \$1,500 wage credit] for a targeted employee who is paid an hourly wage of at least 135% of the minimum wage for more than half of the period involved.)
- Limiting the total amount of all tax benefits available "per employee," in any given year, to the lower of (a) \$10,000 or (b) 20% of the total of the wages paid to the

employee involved and the health insurance premiums paid on behalf of such employee.

- Apply de-certifications for cause to all periods beginning with the earliest documented date of the infraction on which the de-certification is based and require that any benefits received during such period by a decertified firm should be subject to mandatory repayment.

Enforce the 2005 Reforms:

- Ending the current annual boundary amendment process (the "we bring the zone to you" approach) that has opened the operation of many of the state's zones to favoritism and corruption. (NOTE: Currently a bill introduced by Senator George Winner would allow local Zone certification officers to unilaterally make boundary amendments in a way that could undermine this reform.)
- Halting the benefits going to businesses that used re-incorporation and other ruses to get into the program. The 2005 law added a requirement that such firms document that re-incorporations and similar changes were undertaken for a valid business purpose and not just to qualify for empire zone benefits. The NYS Department of Taxation and Finance should enforce this 2005 change in a consistent manner and in the spirit in which it was enacted.
- Tightening the program's certification requirements to ensure that firms that violate (or have, in recent years, violated) labor, health and safety, environmental or other important statutory safeguards are not certified to receive zone benefits; or, if they are already certified, that they lose such certification
- Ensure that the program promotes revitalization of the State's existing cities, towns and villages, efficient use of municipal services and avoids the environmental problems associated with unplanned sprawl development, by limiting zone designations and boundary revisions to areas that are served by public sewer or water infrastructure, previously developed areas, or brownfields (this reform did not seem to be applied to the recent AMD deal where they located the Zone in the middle of a forest not served by municipal services. In fact, this project will require the county to develop a water line to the site in order to provide AMD with over 2 million gallons of water per day).

Finally, NYFF supports removing companies from the program that have not been able to live up to their job creation goals and to further remove companies that have used reincorporation ruses to get in the program to start.

Reform Industrial Development Agencies

8 Simple Reforms to Increase Transparency, Accountability, and Oversight

1. **Ensuring Broader Oversight and Coordination** by enforcing new and more stringent guidelines on board membership. We must ensure that the boards blend business, organized labor, educational, and environmental representatives to ensure the local community to have a say in development. IDAs within the same geographic area (e.g. county, village and city IDAs) must coordinate and approve of any plans which are within their borders.

2. **Community Impact Reports (CIRs)** can be an essential tool for assessing the potential positive and negative impacts a proposed project will have for the local community. The CIR will be an independently conducted study looking into the quality of the jobs created or retained, the effect on housing in the area, the effect on other businesses, the effect on open space and the effect on local infrastructure, such as transportation, schools and water and sewers. Approval should be conditional on the completion of a satisfactory CIR and on an agreement within the contract to address recommendations made in the CIR.

3. **A set of Basic Standards** for businesses applying for IDA assistance should be enhanced. Mandating basic employment, community, civil rights and environmental benefits standards on subsidy deals will ensure that subsidy recipients create quality jobs, meet community needs, and have a positive environmental impact in our neighborhoods. Such standards would include paying a living or prevailing wage, hiring locally when possible, protecting greenfields and community benefits standards. We should further ensure that IDA benefits are not given to firms that violate state laws including those dealing with environmental quality, worker safety, and fraud similar to that governing the Empire Zones.

4. **Improving Reporting Requirements** on subsidy contracts by implementing statewide reporting standards. This would assist local agencies make future subsidy choices by requiring data to be reported on job creation and retention, Payments in Lieu of Taxes (PILOTs) and information on all government assistance provided to a project (not just assistance provided by the IDA).

5. **Requiring Enforceable Clawback Penalties** for IDA recipients who fail to meet the agreed-to contractual obligations. Clawbacks are a type of penalty through which a city or county cancels, reduces, or recovers a subsidy when the recipient fails to deliver on its contract obligations. With stronger reporting requirements, the locality will have the abilities to determine if the business is in breach of contract.

6. **Increasing the Effectiveness of IDA Public Hearings** which currently come at the end of the IDA review process after all of the negotiations between the business and the IDA have already occurred and right before the approval vote is to happen. Often the board members do not show up at the public hearings. The public must be given earlier notice of applications that have been filed with the IDA and some idea as to when those projects are likely to come up for a vote and board member who do not show should not be allowed to cast a vote. A possible model for this is the scoping session requirement under the State Environmental Quality Review Act.

7. **Ensuring that IDAs are run transparently** by requiring each IDA to present records of their standard operations, hearings on deviations and copies of approved deviations are sent at least annually to the state, the chief executives and all board members of affected local governments and that these policies and any changes be made available to the public and posted on the IDA's website. Each IDA should also maintain and make readily available all records of the schedule of PILOT payments, late payments, debts and the allocable taxing jurisdiction. The IDAs should make certain the payments are transmitted to the treasuries of these local governments.

8. **Establishing meaningful penalties for IDAs that violate Article 18-A's anti-piracy provisions.** We must ensure that corporate piracy such as that conducted by the Town of Amherst IDA against the City of Buffalo does not go unpunished. Instead of holding the corporation solely accountable and forcing them to pay back Amherst, a penalty should be assessed on the IDA such as suspension from making deals for a meaningful period of time (six months) and escalate per violation. The return payment should not be made to the locality in violation, but rather to the wronged party. These reforms would hopefully deter violations of article 18-A.

Microenterprise/Entrepreneurial Development

The microenterprise development industry has defined a microenterprise as a business with five or fewer employees requiring \$35,000 or less in start up capital, and does not have access to the traditional commercial banking sector.

Microenterprise development is seen as a holistic approach, embracing poverty alleviation, human development and economic development strategies. For this reason, a wide range of institutions - including stand-alone microenterprise development organizations, community development corporations, organizations with loan funds, community action agencies, women's organizations, community development banks and credit unions, housing and social service programs, and government agencies at the local, state, and national levels - are involved in microenterprise development.

After a decade of operation, microenterprise development programs in the U.S. are creating jobs, generating income, building assets, and enhancing skills. These results are particularly impressive considering the fact that a significant proportion of assisted microentrepreneurs are individuals facing obstacles presented by race, gender, ethnicity, income, and location barriers as well as job market fluctuations. Whether the business is the sole source of family income or a crucial supplement to family earnings, microenterprise development has put many low-income families on the road to self-sufficiency.

By generating new economic activity, microenterprise also increases public tax revenues and private incomes, thereby reducing dependence on public assistance, which in turn helps to shrink public budgets. These significant social and economic benefits far outweigh the cost of public and private investment in microenterprise development.

Why Fund Microenterprise Development? According to the U.S. Census, Microenterprises account for fully 88% of all businesses in NYS and employ approximately 20% of the state's workforce. Sole proprietorships (a business without employees) account for 72% of all businesses in NYS and have had an average annual growth rate of 3.36% between 1997 and 2003 (equates to an average of 45,000 new businesses per year). There are currently 1.6 million microenterprises operating in New York generating approximately \$58 billion in revenues annually. Microenterprise development should be viewed as an economic development priority not an afterthought. The emphasis of New York's economic development policy is on attracting and retaining large businesses while small business development gets only a fraction of the resources.

Empire State Development Corporations Annual Report to the Legislature (2000) on the state funded microenterprise development program suggested the following: State funded programs conservatively generate \$2 in tax revenue for every state dollar invested in the program;

- Program costs the state only \$1,585 per job created (Compared to the Jobs Now Program which averages \$10,000 per job and the Job Development Authority that averages \$35,000 per job);
- Programs should be expanded to areas of the state that currently lack coverage and grants to these training organizations should increase to maximize federal matching dollars.

Small business development is the lifeblood of the New York State economy. The Entrepreneurial Assistance Program (EAP) is one of the most successful small business development programs run by New York State. EAP is operated by the Empire State Development Corporation and provides intensive training and technical assistance to persons wanting to start their own small business. EAP is different than other small business development programs in that it focuses its outreach to women, minorities, individuals with disabilities, and dislocated workers. There are 22 EAP Centers located strategically around the state. These centers provide training that takes participants from the inception of a business idea, through the formulation of a business plan and finally to securing funding for start-up. The technical assistance provided to these businesses does not end when the business is started. EAP centers stay with their start-ups for a period of five years. If the business encounters problems they can always turn to the EAP Centers for assistance.

A 2000 ESDC cost benefit analysis of the program revealed conservatively that New York State received \$2 in personal income and sales tax for every \$1 invested in the program. Every year, without fail, the Governor proposes to eliminate funding for this vital and cost effective program.

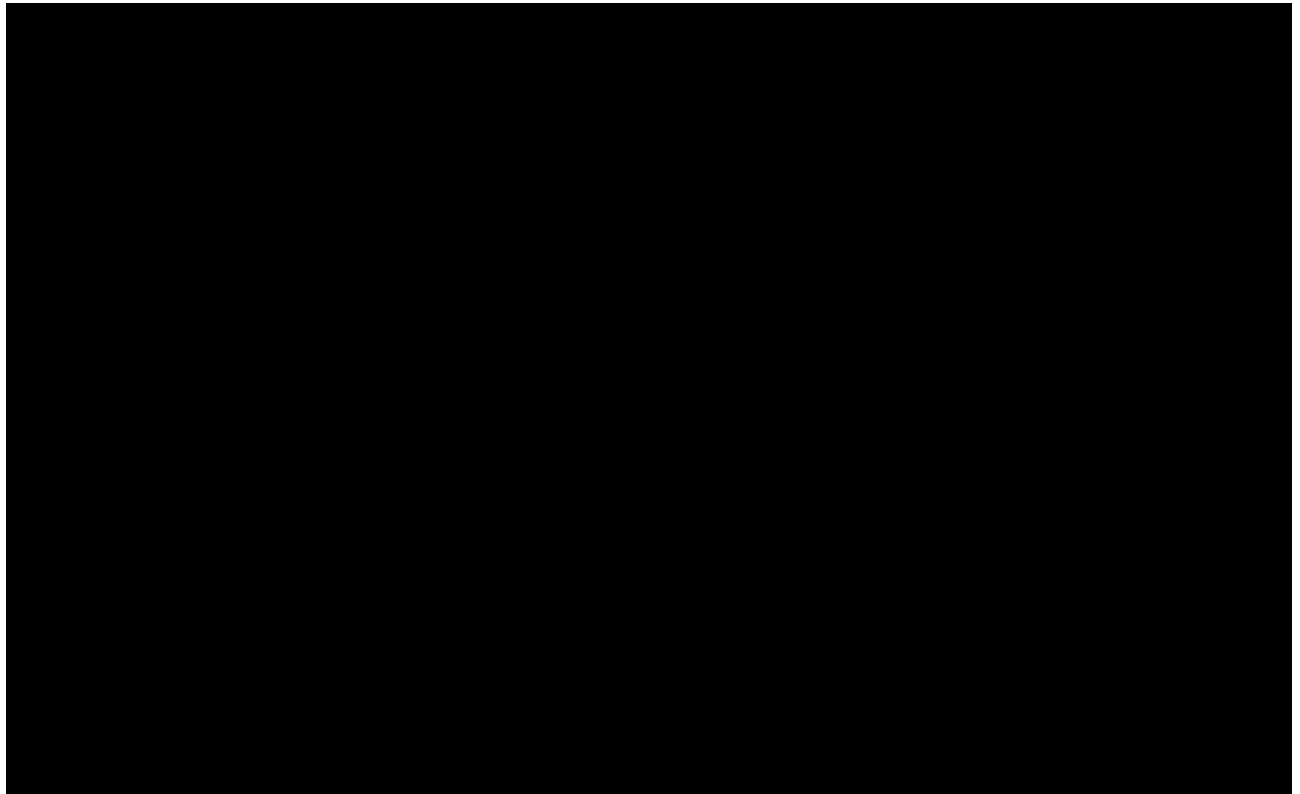
There are also other programs operating throughout the state that are doing incredible work. There are numerous partnerships between Community Loan Funds, CDFIs, Academic Institutions, Community Action Programs, Community Development Corporations, County Governments, Credit Unions, Banks, and other microenterprise development organizations. These partnerships allow organizations to maximize community resources and avoid duplication of services.

**Sole-Proprietorships in New York:
A Growing and Increasingly Significant
Part of New York States Economy**

Year	Sole-Proprietorships	% Increase from previous year
2002	1,302,672	3.40%
2001	1,258,822	4.60%
2000	1,202,943	2.90%
1999	1,168,595	2.70%
1998	1,137,871	3.20%
1997	1,101,776	

Sole-proprietorships in New York constitutes over 72 percent of all businesses. The total number of sole-proprietorships has increased an average of 3.36 percent each year since 1997; that's about 45,000 new businesses opened per year. Growth in sole-proprietorships has remained steady, and actually increased, during the 2001-2002 recession. In 2002 alone, New York Sole Proprietorships reported 58.7 billion dollars in receipts. This portion of the workforce is much too large and important to the New York State economy to be ignored.

**Percentage Change in Employment by Business
Size***



Initiate a \$20 Million Statewide Microenterprise Technical Assistance and Lending Development Fund

The state should develop a new funding mechanism to support microenterprise training, TA and lending. This fund could be operated through Empire State Development Corporation (ESDC) and should be made available to all microenterprise development organizations through a statewide RFP. Regionally based training focused and lending focused organizations should work together to develop collaborative partnerships to meet the needs of local entrepreneurs. This program should replace the Entrepreneurial Assistance Program as the primary funding source for microenterprise development organizations in NYS. The EAP program, while extremely effective, has been underfunded since its inception and has severely limited the number of organizations that have access to the funding. Based on past research on the efficacy of EAP and other microenterprise development programs NYS should invest a minimum of \$20 million in SFY 07-08 to ensure adequate funding for these needed services. Conservative estimates based on prior ESDC research would indicate that the state would see \$40 million in tax revenue generated by the new businesses created with this program.

Individual Development Accounts (IDAs)

Many Americans work hard to get an education, purchase a home, or start a business. But they usually have help along the way from family, professional networks, and the myriad other opportunities that come with economic advantage. Even the federal government subsidizes asset accumulation for the non-poor via mortgage interest deductions, preferential capital gains, and pension fund exclusions. For the significant number of Americans who lack the resources to take advantage of those opportunities, basic goals like education, home ownership, and meaningful employment remain an elusive dream.

IDAs are dedicated savings accounts similar in structure to IRAs. Generally, the account holder chooses to save toward one of three goals: purchasing a first home, continuing education or job training, or starting or expanding a small business. Community development organizations use funds from public and private sources to match the account holder's deposits. Within a few years, the account holder can accumulate sufficient assets to invest in the chosen goal. In addition to matching funds, account holders receive credit counseling, help with budgeting, and economic literacy training.

IDA programs have varying levels of eligibility requirements. Some include households living at less than or equal to 150 percent or 200 percent of the federal poverty level, while others require that the account holder's household income not exceed 80 percent of the area median income. Organizations also determine eligibility for IDA programs using household net worth. IDAs are designed to help individuals and families who have both low income and low assets. Funds from government appropriations and private sources match the account holder's deposits at a rate ranging from 1:2 to 9:1. Programs place limits on the amount that will be matched each year.

Asset-building strategies represent an increased emphasis on developing self-sufficiency. Some IDA holders rely on public assistance. Traditional public assistance programs address only income maintenance and consumption. Such programs do not support the transition

to self-sufficiency, and strict asset limits for recipients of public assistance create a barrier to savings. Asset-building programs complement income maintenance programs by providing a realistic vehicle through which individuals and families can improve their economic well-being. Many of the IDA holders who participate in income maintenance programs will be able to move off public assistance.

New York State currently allows individuals to open IDA accounts, but the State does not provide funding. Although New York legislators voted to disregard funds in TANF recipients' IDA accounts when determining eligibility for public assistance, New York has no comprehensive IDA legislation. New York continues to lag many other states in the support of Individual Development Accounts.

A number of other states have made significant strides in developing IDA programs. Indiana has backed its IDAs with \$6.5 million from the state general fund and another \$500,000 annually in tax credits to contributors to an IDA program. Anyone who contributes to an Indiana IDA will receive a fifty percent tax credit on contributions between \$1,000 and \$50,000. The match rate is 6:1 total, composed of 3:1 by the state and 3:1 required of administering organizations. In Pennsylvania, the State has appropriated \$1.25 million for a Family Savings Account program. North Carolina has appropriated \$300,000 a year for the next two years for IDAs, and the State has set aside \$250,000 of Community Development Block Grant funds for home ownership IDAs. Iowa has allocated \$50,000 to support a five-year demonstration known as the Family Investment Program. Other states give tax benefits to contributors to IDA programs. A total of more than forty community-based organizations and twelve states are running or supporting IDA programs.

At the federal level, Congress has passed the Assets for Independence Act. The Assets for Independence Act set up a national IDA demonstration project, funded over four years with \$100 million. In order to access these funds states and local groups must provide a non-federal match.

Children's Savings Accounts – Sowing the SEEDs of Change

The Harlem Children's Zone has also just launched a new project offering SEED Accounts. Savings for Education, Entrepreneurship and Downpayment (SEED) accounts are similar in structure to IDAs but are focused on helping children build assets. SEED accounts can make a substantial difference in the life a child by helping them accumulate assets for when they become adults. They will have been able to save thousands of dollars for the purpose of purchasing a home, starting a business or getting a college education. These programs will also work with the children to give them the educational tools they need later in life that will help them not only manage money but their future as well.

The Harlem Children's Zone is one of only a few organizations nationally chosen to offer these accounts as part of a demonstration project. The Harlem Children's Zone intentionally develops programs where other agencies are not located and poor children and families have no where else to turn for help. The Harlem Children's Zone is offering SEED accounts to Children in its Harlem GEMS Universal Pre-Kindergarten Program.

Active IDA Programs in New York State

Affordable Housing Partnership, Albany
Alternatives Federal Credit Union, Ithaca
Brooklyn Ecumenical Credit Union, Brooklyn
Challenge Industries, Ithaca
Chautauqua Opportunities Inc., Dunkirk
Genessee Co-Operative Federal Credit Union, Rochester
Homesteaders Federal Credit Union, Manhattan
Lower East Side Peoples Federal Credit Union, Manhattan
Mount Hope Housing Company, Bronx
Neighborhood Housing Services, Brooklyn
Neighbors Helping Neighbors, Brooklyn
New York Association for New Americans, Manhattan
NEXUS Project/NYC Partnership, Manhattan
Northfield Local Development Corporation, Staten Island
PEACE Inc. (Onondaga CAP Agency), Syracuse
SEEDCO/Non-Profit Assistance Corporation, Manhattan
St. John United Federal Credit Union, Buffalo
Westchester Housing Fund, Hawthorne
Westchester Residential Opportunities, White Plains
Wildcat Services Corporation, Manhattan
YWCA of Rochester and Monroe County, Rochester

Note: There are numerous other programs in the developmental stages throughout the state.

Policy Recommendation:

The Governor and the Legislature should allocate \$5 million in economic development funds to foster the promotion and creation of IDAs. These funds should be used for a pilot project to provide funding to existing IDA programs and to create new programs.

Community Development Financial Institutions (CDFIs)

CDFIs are diverse organizations that meet a need for credit and financial services in disinvested and low wealth communities. A CDFI is a financial institution with a primary mission of community economic development, providing credit and/or investments in urban, rural, and reservation-based communities inadequately served by banks. There are six basic types of CDFIs: community development credit unions, banks, loan funds, micro-enterprise funds, community development corporation-based lenders and venture funds. CDFIs offer loans and savings opportunities to small and micro-businesses, first-time homebuyers, organizations developing affordable housing or community facilities and individuals seeking to improve their economic options.

A distinguishing feature of a community development financial institution is community control of local investment. Community ownership and control allow these institutions to be more responsive to the needs of their members and therefore effective in their lending

and investment strategies. Because of this community control, the commitment to the neighborhoods and consumers they serve will endure.

New York CDFI Facts and Figures

The **106 CDFIs** in New York State have almost **\$676 million in financing** outstanding. New York CDFIs serve predominantly low-income individuals (77.1%), minorities (70.5%) and women (59%). In just one year, CDFIs in New York:

Provided asset-building savings and financial services to more than 64,000 people.
Closed more than 8700 loans and investments
Financed 887 businesses and microenterprises, creating and supporting 2,673 jobs.
Created or renovated 11,621 affordable housing units

Our research indicates for every \$1 of state investment, CDFIs are able to leverage up to \$24 in federal and private sector funding. Thus, a dedicated state fund that allows CDFIs to raise state capital will vastly expand the level of lending and financing services that they are able to provide throughout the state. We also believe a dedicated fund will enable new CDFIs to form in areas that lack adequate service and existing CDFIs to expand their activities to reach more communities.

Policy Recommendations:

NYS should support its recently passed independent New York State CDFI Fund to make investments in CDFIs for a broader range of financing and financial services purposes. We urge the Legislature to support a **\$20 million appropriation** and an expansion of eligible financing activities. We further believe that the fund should be increased to allow for larger grant amounts (going from the current maximum of \$50,000 to \$100,000) that would help leverage additional federal capital and increase the return on the application process).

The New York Legislature worked with the CDFI Coalition to establish the New York CDFI program housed at Empire State Development Corporation in 1997. This program has funded in excess of \$8 million to 35 CDFIs statewide (through 2004) for business lending. Funding under this program has enabled CDFIs to significantly increase lending to minority and women-owned businesses by community development credit unions, loan funds, and banks.