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The New York Tax Windfall

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I. Introduction

1986 was the year of the Great Tax Revolution. After thirty-two years, Congress replaced the 1954 Internal Revenue Code with the 1986 Internal Revenue Code.[1] Congress' avowed purpose in overhauling the Tax Code was to lower tax rates for individuals[2] and corporations,[3] while simultaneously eliminating many tax deductions,[4] credits[5] and exclusions.[6] These changes will cause dislocation and alteration in the economy of the United States,[7] and only time will tell whether the overall effect will be positive.

This trade-off between lowered tax rates and the elimination of deductions, credits and exclusions has the effect of broadening the federal definition of taxable income. Since New York generally follows the federal definition of taxable income,[8] its taxable base will be significantly increased. Thus, unless New York's tax rates

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1. Tax Reform Act of 1986, Pub. L. No. 99-514, 1986 U.S. CODE CONG. & ADMIN. NEWS, 99 Stat. 1 (Oct. 22, 1986) [hereinafter 1986 Reform Act]. Moreover, the Internal Revenue Code of 1954 [hereinafter I.R.C. (1954)] was redesignated as the Internal Revenue Code of 1986. *See* 1986 Reform Act § 2, at 11.

2. Prior to the 1986 Reform Act, individual rates consisted of up to 15 brackets, with a maximum rate of 50%. I.R.C. § 1 (1954). The 1986 Reform Act lowers these rates in two stages. In 1987 there is a transitional 5 bracket rate schedule ranging from 11% to 38 1/2%. After 1987, there will be only two rates, 15% and 28%; however, there will be a 5% surcharge at certain income levels, effectively producing a 33% rate bracket. 1986 Reform Act § 101, at 12-15.

3. Corporate rates have been lowered from a maximum of 46% in 1986 to 34%. 1986 Reform Act § 601, at 165.

4. For example, the two-earner deductions by married couples for tax years after 1986 was repealed. 1986 Reform Act § 131, at 29.

5. For example, the regular investment credit was repealed. 1986 Reform Act § 211, at 82-86.

6. For example, the exclusion of $100 ($200 on a joint return) from the income of an individual for dividends was eliminated. 1986 Reform Act § 612, at 166-67.

7. *See* Hershey, Jr., *Tax Overhaul Reshaping Investment*, N.Y. Times, Nov. 16, 1986, § 12 (Business) at 5, col. 1.

8. N.Y. TAX LAW § 612 (McKinney 1975).

are commensurately reduced, New York will reap a substantial tax windfall, resulting in an estimated overall tax increase of over two billion dollars per year for individuals and two hundred million dollars per year in the case of corporate taxpayers.[9] This expanded definition of taxable income would have an even greater impact upon New York City residents who—in addition—would similarly face higher city income taxes as well.[10]

New Yorkers pay a myriad of local taxes, including: sales and use tax,[11] gasoline and motor fuel tax,[12] cigarette and tobacco tax,[13] stock transfer tax,[14] real estate transfer tax,[15] and auto registration tax[16] just to name a few. Most of these taxes are principally consumption-oriented, or involve some service or use. The New York income,[17] gift and estate taxes,[18] however, are basically imposed for the privilege of living or dying in New York; it is when these taxes become oppressive that residents decide to "bail out" to more understanding jurisdictions. This Article will focus on the cumulative effect of the New York income, gift and estate taxes upon its residents, and conclude that all new income—whether from investment or services—be taxed in the same manner and at lower rates.

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9. *See Now Simplify the State Tax*, N.Y. Times, Sept. 29, 1986, at A14, col. 1. Indeed, it has been reported that "[w]ithout modification of the [New York] State tax structure the 1987 'windfall' will equal an additional $2.4 billion.[sic] composed of $2.2 billion in income tax yield and an increase of $200 million in corporate tax collections. The total grows to $2.8 billion in 1988 if current rates were to continue." E. Brown, II, *Special Feature: New York's Legislative Response To The Tax Reform Act of 1986*, N.Y. St. B.J., Dec. 1986, at 37-38; *see also* Nagourney, *Big Hike In State Bills*, N.Y. Daily News, Sept. 28, 1986 (Business), at 10, col. 5. Approximately 35 states have income taxes keyed to the federal income tax; and, thus, will also receive substantial increases in revenue by the 1986 Reform Act. *See* Herbers, *Local Government in U.S. is Reshaped by Federal Moves*, N.Y. Times, Nov. 30, 1986, § 1, at 1, col. 2. "According to the National Governors Association, the 'tax revolt' by voters is very much alive at the state level and most officials are therefore in favor of reducing state tax rates." *Id.* at 36.

10. New York City also generally follows the federal and state definitions of "Taxable Income." *See* N.Y.C. Admin. Code § 11-1712 (1986). It has been estimated that New York City will also collect at least an additional 250 million dollars in income taxes each year as a result of the expanded definition of taxable income by the Tax Reform Act of 1986. *See* Nagourney, *Big Hike In State Bills*, N.Y. Daily News, Sept. 28, 1986 (Business), at 10, col. 5.

11. N.Y. Tax Law §§ 1101-1148 (McKinney 1975).

12. N.Y. Tax Law §§ 282-289-F (McKinney 1986).

13. N.Y. Tax Law §§ 470-482 (McKinney 1975).

14. N.Y. Tax Law §§ 270-281-a (McKinney 1986).

15. N.Y. Tax Law §§ 1400-1410 (McKinney 1975).

16. N.Y. Tax Law §§ 1132-1214 (McKinney 1975).

17. N.Y. Tax Law §§ 601-698 (McKinney 1975).

18. N.Y. Tax Law §§ 951-963 (McKinney 1975).

II. New York Income Tax

The State of New York imposes an income tax on its residents[19] and, to a limited extent, on its non-residents.[20] This Article will focus only on resident taxpayers.

A. Who is a Resident?

For income tax purposes, a New York resident is a person who: (1) is domiciled in New York;[21] or (2) is domiciled elsewhere, but maintains a permanent place of abode in New York and spends, in the aggregate, more than 183 days of the taxable year in the state.[22]

B. Different Tax for Differing Income

The tax rates for residents vary depending upon whether the income is derived from personal services[23] (earned income) or through investments[24] (investment income). The maximum New York State income tax rate for earned income in 1987 is nine percent,[25] while investment income can be taxed as high as thirteen percent.[26]

Why does this bias exist against income through investment? Why do we impose a penalty against investment income? Why do we discriminate against the frugal, retirees, widows and orphans, to name a few? Perhaps the answer is that it is more politically palatable to tax investment income than earned income. Regardless of the morality or fairness of such a premise, however, political furor is sure to escalate as the 1986 Reform Act (and therefore, the New

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19. N.Y. TAX LAW §§ 601, 611 (McKinney 1975).

20. Non-residents of New York are generally taxed only on income derived from New York sources. *See* N.Y. TAX LAW §§ 601, 631, 632 (McKinney 1975).

21. *See* N.Y. TAX LAW § 605(a)(1) (McKinney 1975). If this domiciliary, however, maintains no permanent place of abode in New York and maintains a permanent place of abode elsewhere, he is not considered a domiciliary for New York income tax purposes unless he spends more than 30 days of the taxable year in New York. *Id.*

22. *See* N.Y. TAX LAW § 605(a)(2) (McKinney 1975). If such non-domiciliary, however, is in the armed forces of the United States during an induction period, he is not considered a resident for income tax purposes despite his physical presence in New York. *See id.* New York City has a definition, for tax purposes, of "resident" similar to New York State's definition. *See* N.Y.C. ADMIN. CODE § 11-1705 (1986).

23. *See* N.Y. TAX LAW § 603-A(b)(1) (McKinney 1975 & Supp. 1987).

24. *See* N.Y. TAX LAW § 602 (McKinney 1975).

25. *See* N.Y. TAX LAW § 603-A(a)(2) (McKinney 1975 & Supp. 1987).

26. *See* N.Y. TAX LAW § 602(g) (McKinney 1975 & Supp. 1987). This is particularly burdensome in the case of dividend income, which is derived from income that has already been taxed at the corporate level. *See* C. Katsoris, *The Double Jeopardy of Corporate Profits*, 29 BUFFALO L. REV. 1 (1980).

York tax base) expands the definition of taxable income[27] by eliminating many deductions, exclusions and credits that previously sheltered the taxation of investment income.[28] This removal will no doubt raise the political awareness of investing taxpayers as to the differing tax rates based solely on the source of the income. This increased concern will be a particular problem in the case of long-term capital gains, which will become fully taxable with the repeal of the net capital gain deduction.[29]

C. New York's Income Tax Compared to That of Neighboring States

New York has the highest average per-person income tax levy of any state in the country.[30] This dubious distinction will be further exacerbated by the fact that many states, unlike New York, do not follow the federal definition of taxable income.[31] Thus, the Tax Reform Act of 1986 will not increase their taxable base, as it will in the case of New York.[32]

Moreover, New York's top income tax rates of thirteen percent for investment income and nine percent for earned income[33] generally far exceed the rates imposed by New York's neighbors.[34] For example, Connecticut has no general personal income tax.[35] New Jersey has a maximum personal income tax rate on its residents of *only* three and one-half percent,[36] while Pennsylvania currently has an

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27. *See supra* notes 8-10 and accompanying text.

28. *See supra* notes 2-6 and accompanying text.

29. Prior to the Tax Reform Act of 1986, individuals, estates and trusts could deduct 60% of their net capital gain (excess of net long-term capital gain over net short-term capital loss) from gross income. I.R.C. § 1202 (1954). This deduction, however, was repealed by the Tax Reform Act of 1986. *See* 1986 Tax Reform Act § 301(a), at 132.

30. *See* Shribman & Murray, *Loss of Sales-Tax Deductions in Overhaul Bill Is Expected to Prompt Revisions in State Codes*, Wall St. J., Aug. 27, 1986, at 38, col. 1. The District of Columbia has a higher average per-person income tax levy than does New York. *See id.* In 1985, approximately 59% of New York's revenue was derived from the state income tax. *State and Local Taxes*, J. ACCOUNTANCY, Oct. 1986, 30, 31. Moreover, during the fiscal year of 1984, New York taxpayers bore the fourth highest overall per-capita state tax burden in the country. 47 State Tax Review (CCH) No. 3, at 1 (Jan. 21, 1986).

31. *See supra* notes 8-10 and accompanying text.

32. *Id.*

33. *See supra* notes 23-26 and accompanying text.

34. *See infra* notes 35-59 and accompanying text.

35. CONN. GEN. STAT. ANN. § 12-506 (West 1983 & Supp. 1986) (currently provides for taxing net capital gains at 7% rate and certain dividend and interest income at rates of up to 12%). *See* 1986 Conn. Acts 86-397 (Reg. Sess.).

36. *See* N.J. STAT. ANN. § 54A:2-1 (West 1986).

income tax rate of slightly over two percent.[37] Finally, Vermont[38] and Massachusetts[39] (which border on the more sparsely developed regions of New York) have personal income tax rates more favorable than the New York rate.

III. New York Estate Tax

In addition to the income tax, New York imposes an estate tax[40] on its residents[41] and, to a limited extent, on its non-residents.[42] This Article will focus only on the estates of resident decedents. Unlike the definition of residency for income tax purposes,[43] the term resident for New York estate purposes is synonymous with the decedent's domicile.[44] The elements of domicile are the decedent's manner of living and his or her actual intent and conduct.[45] In this regard, although maintaining a permanent place of abode or spending more than 183 days[46] of the taxable year within the state do not

37. *See* PA. STAT. ANN. tit. 72, § 7302 (Purdon 1968 & Supp. 1986) (*amended by* 1986 Pa. Legis. Serv. 77 (Purdon)).

38. Vermont is expected to impose a 1987 income tax rate of 25.85% of federal income tax liability. *See* 47 State Tax Review (CCH) No. 47, at 1 (Nov. 25, 1986). In view of the new top federal personal income tax rate of 28%, the highest Vermont personal income tax rate may be estimated at slightly over 7%. *See id.*

39. Massachusetts imposes a 10% rate on investment income (taxable interest, other than from Massachusetts savings institutions, dividends and net capital gains) and 5% on all other taxable income (including earnings). *See* MASS. ANN. LAWS ch. 62, § 4(a) & (b) (Law. Co-op. 1978). A slight additional surcharge has been phased out. *See* 1985 Mass. Adv. Legis. Serv. ch. 593, §§ 38, 44 (Law. Co-op).

40. An estate tax is a form of death tax. *See* I.R.C. § 2011 (1954). It is computed on decedent's estate as a whole instead of separately on each beneficiary's share of the estate, as is the procedure with an inheritance tax. *See* I.R.C. § 2001 (1954).

41. *See* N.Y. TAX LAW § 952 (McKinney 1975 & Supp. 1987).

42. *See* N.Y. TAX LAW § 960 (McKinney 1975 & Supp. 1987). Generally, only real or tangible personal property of a non-resident decedent situated in New York is subject to the New York estate tax. *See id.*

43. New York Tax Law § 650 defines a resident individual for income tax purposes, but does not apply to the New York estate tax. *See In re* Daly's Estate, 178 Misc. 943, 36 N.Y.S.2d 954 (Sur. Ct. N.Y. County 1942).

44. *See* 2 H. HARRIS, ESTATES PRACTICE GUIDE § 617 (3d ed. 1968); New York Times, Nov. 27, 1975, at A44, col. 1; *see also* H. GOODRICH & E. SCOLES, CONFLICT OF LAWS § 29 (4th ed. 1964).

45. The place of domicile is a question of fact, to be determined from a consideration of such factors as where the decedent voted; where he conducted his principal business activities; the center of his social affairs; the place he referred to as home; where he lived the greatest portion of time; the location of his principal possessions; where he paid local taxes. *See* 2 New York Tax Reports (CCH) §§ 88-105 (May 1984). No single factor is controlling, and the decedent's intention must be ascertained from the overall set of facts. *See id.*

46. See *supra* notes 21, 22 and accompanying text for a discussion of the term "resident" for income tax purposes.

in and of themselves constitute domicile, such contacts would obviously be most important factors in the determination of domicile.[47]

Some states, such as Florida,[48] limit their death tax to only the extent of the federal state death tax credit[49] (state tax credit). Thus, Florida's death tax is characterized as a "slack" tax or "sponge" tax because it fills the gap of the state tax credit.[50] If there is no state tax credit, there is no slack or sponge tax. Accordingly, the slack or sponge tax is whatever the state tax credit allows, and since the credit reduces the federal estate tax due, there is no additional cost to the taxpayer's estate. For example, in 1987, when a taxable estate of $600,000 would be sheltered from the federal estate tax because of the unified credit,[51] there would be no state tax credit and, therefore, no Florida death tax.[52]

The New York estate tax, however, is not computed with reference to the state tax credit. Thus, one can incur a New York estate tax, even though there may not be a federal estate tax due. This result is attributed to the fact that although many of the New York estate tax provisions mirror the federal estate tax,[53] the New York estate credit[54] is not nearly as generous as that which is available under the federal unified credit.[55] Thus, in a Florida estate of $600,000 there would be *no* federal estate tax (because of the unified credit) and *no* Florida death tax (since it cannot exceed the state tax credit, which in this case is zero).[56] Yet, in a New York estate of $600,000

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47. *See* 2 New York Tax Reports (CCH) § 88-105 (May 1984).

48. FLA. CONST., art. VII, § 5 (1970 & Supp. 1986); *see* 2 State Tax Guide (CCH) § 89-336 (Oct. 1985).

49. I.R.C. § 2011 (1986). This section permits a credit against the federal estate tax, but limited to a percentage of the adjusted taxable estate, ranging from 8/10 of 1% to 16% for amounts in excess of $10,040,000. *See id.*

50. Other states that apply the slack tax concept are Alabama, Alaska, Arizona, Arkansas, Colorado, Georgia, Maine, Mississippi, Missouri, New Mexico, North Dakota, Oregon, Texas, Utah, Vermont, Virginia and Wyoming. *See* U.S. Tr. Monthly Rptr., May, 1982, at 1-2.

51. Section 2010 of the Internal Revenue Code of 1986 provides for a unified credit against the federal gift or estate tax. For decedents dying after 1986, the unified credit is $192,800 (§ 2010(a)), which is the tax on the first $600,000 under the rate schedule provided under I.R.C. § 2001(c).

52. *See* U.S. Tr. Monthly Rptr., May, 1982, at 1. Moreover, the state tax credit shall not exceed the amount of the federal estate tax due, reduced by the unified credit. I.R.C. § 2011(f) (1986).

53. *See* N.Y. TAX LAW §§ 954, 955 (McKinney 1975 & Supp. 1987).

54. The maximum credit against the New York estate tax is $2,750. *See* N.Y. TAX LAW § 952(b) (McKinney 1975 & Supp. 1987).

55. *See* I.R.C. § 2010(a) (1986). For decedents dying after 1986, the federal estate tax unified credit is $192,800. *See* I.R.C. § 2010(a) (1986).

56. *See supra* notes 48-52 and accompanying text.

there could be a New York estate tax of $25,500.[57]

Furthermore, in a New York estate—even when there is a federal estate tax—the New York estate tax rates can exceed the federal state tax credit by as much as five percent.[58] No such excess occurs in a slack or sponge tax jurisdiction, because in those jurisdictions, the state death tax will never exceed the state tax credit.[59]

IV. Tax Brinksmanship

New York has the highest average per-person income tax levy[60] and among the most unfavorable death tax provisions of any state in the country.[61] To assert that these high tax rates do not dissuade businesses from moving or remaining here, or discourage retirees from migrating elsewhere, is to defy logic.[62] Although the New York economy has been relatively strong during the last few years,[63] New York cannot afford to become indifferent or complacent.[64]

Unfortunately, New York State and New York City have played this game of tax brinksmanship before. In 1975, as part of the legislative efforts to prevent default by New York City, a New York City estate tax was enacted to take effect on April 1, 1976. It was

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57. The New York estate tax on a taxable estate of $600,000 would be $26,000, *see* N.Y. TAX LAW § 952(a)(4) (McKinney 1975 & Supp. 1987), less a unified credit of $500.

58. The New York estate tax rate is 21% for amounts over $10,100,000, *see* N.Y. TAX LAW § 952(a)(4) (McKinney 1975 & Supp. 1987), whereas the maximum amount allowed under the federal estate tax for the state tax credit is only 16%. *See* I.R.C. § 2011(b) (1986).

59. *See supra* notes 48-52 and accompanying text.

60. *See supra* notes 30-32 and accompanying text.

61. *See supra* notes 48-59 and accompanying text.

62. *See* E. Brown, II, *Special Feature: New York Legislative Response to the Tax Reform Act of 1986*, N.Y. ST. B.J., Dec. 1986, at 37; Goodman, *Cuomo's Insufficient Tax Cuts*, N.Y. Times, Dec. 12, 1986, at A31, col. 1; *Now Simplify the State Tax*, N.Y. Times, Sept. 29, 1986, at 14, col. 1.

63. *See* Hershey, Jr., *Unemployment Rate Remains 6.9% Despite Rapid Creation of New Jobs*, N.Y. Times, Dec. 6, 1986, at 56, col. 1; Reid, *November Jobless Rate Declines In New York City and New Jersey*, N.Y. Times, Dec. 6, 1986, at 56, col. 5.

64. For example, modern technology would permit the stock exchanges and brokerage houses to transfer substantial parts of their business outside the City and State of New York. *See* Katsoris, *City's Death Tax and Its Possible Effects*, N.Y.L.J., Jan. 29, 1976, at col. 4, *reprinted at* 379 N.Y.S.2d (No. 1) 15, at 21 (Mar. 9, 1976). During the period from 1969 to 1974, there was a loss of approximately 339,000 jobs in New York City, including a loss of some 35,000 jobs in the securities and commodities trading industries alone. *See* New York Times, Dec. 6, 1975, at A60, col. 5.

to be the only municipal estate tax in the nation.[65] Despite New York City's financial plight, such a tax would have been counterproductive. Simply put, no one was going to pay up to 10.5% of his estate for the privilege of dying in the City of New York.[66] The legislature, to its credit, realized the impracticality of such a tax and repealed it before it ever took effect.[67]

As to our present tax structure, we must admit that New York is not an attractive state for business. The fact remains that when the Reform Act is fully effective, New York will have a maximum income tax rate (thirteen percent for investment income) of almost one-half the federal rate of twenty-eight percent. Moreover, New York City residents, who are also subjected to a maximum city tax rate in excess of four percent,[68] will face combined top rates amounting to almost two-thirds of the top federal rate.

Admittedly, state income taxes are still deductible from the federal rates;[69] however, the after-tax cost of state income taxes will have risen because their deductibility will have less effect. For New Yorkers receiving investment income, the news is even worse. For example, a widow, widower, orphan or retiree receiving investment income—including capital gains—will be taxed at a rate of up to thirteen percent. Moreover, if they die in New York, their estates face a potential shortfall of five percent against the federal state tax credit.[70] Finally, if they set up trusts in New York, the high New York income tax rates would generally continue on these trusts long after the decedent's death.[71] If one compares New York to Florida, which imposes no income tax (investment or earned)[72] and no death tax

65. *See* RIA, Tax Coordinator, Weekly Alert, Dec. 4, 1974, at 3; *see also* Wall St. J., Dec. 17, 1975, at 1, col. 5.

66. Since the upper brackets of the New York estate tax reach 21%, the proposed 50% New York City estate tax surcharge on the New York State estate tax would have equaled 10.5%; and, since the limits of the federal state tax credit would have already been exceeded by the New York State estate tax, the 10.5% loss would be a net loss. *See* Katsoris, *City's Death Tax and Its Possible Effects*, N.Y.L.J., Jan. 29, 1976, at 1, col. 4, *reprinted at* 379 N.Y.S.2d No. 1, 15, 20 (Mar. 9, 1976); *see also* ASSOCIATION OF THE BAR OF THE CITY OF NEW YORK BULLETIN, at 57 (Apr. 15 1976).

67. *See* S. Weisman, *Rise in Estate Tax in New York Voided*, N.Y. Times, May 28, 1976, at A1, col. 8.

68. *See* N.Y.C. ADMIN. CODE § 11-1702 (1986); 1986 N.Y. Laws 222, 253; 1985 N.Y. Laws 364.

69. I.R.C. § 164(a)(3) (1986).

70. *See supra* note 58 and accompanying text.

71. *See* N.Y. TAX LAW § 605(c) (McKinney 1975) (resident estate or trust).

72. FLA. CONST., art. VII, § 5 (1970 & Supp. 1986); *see* 1 State Tax Guide (CCH) at 1501 (Oct. 1985).

in excess of the federal state tax credit,[73] one wonders why anyone retires in New York.

"In an economy where people and businesses are free to wander, individual states cannot afford to stray very far from the national consensus on tax equity."[74] New York simply cannot risk an exodus by its middle class and wealthy citizens because such an exodus would eventually undermine its social and economic stability.

V. Legislative Proposals

With the approach of the 1987 automatic increase in New York income taxes,[75] numerous suggestions have been made for dealing with the tax windfall.[76] Although one would expect that many adjustments will be made during the process of political compromise, two major plans have surfaced which deserve discussion. While one has been proposed by New York's Governor, Mario Cuomo (Governor's Plan),[77] the Republican majority in the New York Senate has proposed another (Republican Plan).[78]

The Governor's Plan is narrow in scope and is based upon the premise that the tax windfall to New York will be only about $1.7 billion per year.[79] Accordingly, his plan still leaves the 1987 maximum rates on earned income at nine percent and investment income at thirteen percent.[80] It does, however, widen the tax brackets, limit capital gains taxes to nine percent, create a new deduction for two-income households and increase tax credits and the standard deduction that would remove many working poor from the tax rolls.[81]

The Republican Plan is much broader. When fully effective it would save New York taxpayers about $4.5 billion annually.[82] Thus,

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73. *See supra* notes 48-52 and accompanying text.

74. *Now Simplify the State Tax*, N.Y. Times, Sept. 29, 1986, at A14, col. 2.

75. *See supra* notes 1-9 and accompanying text.

76. *See Now Simplify the State Tax*, N.Y. Times, Sept. 29, 1986, at A14, col. 1. Suggestions for handling the tax windfall have varied from an income tax cut to the granting of a temporary rebate, lowering the sales tax, and funding additional spending programs. *See id.*

77. *See* Schmalz, *Revision Made In Cuomo Plan On State Taxes*, N.Y. Times, Dec. 11, 1986, at B1, col. 5.

78. *See id.* at B2, col. 1.

79. *See id.*

80. *See id.* at B1-B2. Moreover, although the Governor's Plan also reduces the maximum tax rate to 9 percent for investment income other than capital gains (i.e., dividends and interest), it does so only for those taxpayers with incomes between $35,000 and $80,000. *Id.* at B1, col. 5.

81. *See id.*

82. *See* Goodman, *Cuomo's Insufficient Tax Cuts*, N.Y. Times, Dec. 10, 1986, at A31, col. 2.

it not only seeks to return the so-called tax windfall, but, in addition, offers an actual tax cut.[83] Basically, the Republican Plan eliminates the distinction between earned and investment income and proposes a tax on all income below $30,000 at four percent, and thereafter at a maximum rate of *only* seven percent.[84]

Although both plans are a step in the right direction in that they seek to neutralize the tax windfall, the Republican Plan is preferable. The Governor's Plan is very narrowly targeted. Basically, it freezes the maximum rates to their present levels while retaining some bias between earned and investment income. Thus, New York is locked into its present uncompetitive position with its neighboring states.[85] On the other hand, the Republican Plan is far broader and seeks to make New York a more attractive state in which to live and do business.[86] New York simply cannot afford merely to preserve the present status quo offered by the Governor's Plan.

Once a consensus is formulated as to the extent to which tax relief is granted, a review should also be made of the method by which the New York income tax is to be collected.[87] Several methods have been suggested—each with its advantages and drawbacks.[88] The legislature should select the method most favorable to the state, and then seek to implement it as part of an overall tax reform.

83. *See id.*

84. *See First, Stop the Tax Windfall*, N.Y. Times, Dec. 12, 1986, at A34, cols. 1-2; Schmalz, *Revision Made In Cuomo Plan On State Taxes*, N.Y. Times, Dec. 11, 1986, at B2, col. 1.

85. *See First, Stop The Tax Windfall*, N.Y. Times, Dec. 12, 1986, at A34, col. 2.

86. *See id.*

87. *See* E. Brown, II, *Special Feature: New York Legislative Response to the Tax Reform Act of 1986*, N.Y. St. B.J., Dec. 1986, at 37.

88. *See Now Simplify The State Tax*, N.Y. Times, Sept. 29, 1986, at A14, col. 1. "Now suppose New York shifted tactics and tied its income tax not to the federal definition of taxable income but to the bottom-line amount that a taxpayer owes the Feds. Instead of demanding, say, 9 percent of federally computed income, New York could ask for, say, one-third of whatever amount an individual owes to Washington. This fraction could be adjusted to generate whatever level of revenue Albany deems necessary." *Id. But see* E. Brown, II, *Special Feature: New York Legislative Response to the Tax Reform Act of 1986*, N.Y. St. B.J., Dec. 1986, at 37. "Any benefits, however, are outweighed by its disadvantages. It would not be as simple as it sounds because taxpayers would have to make several adjustments to their federal computations to account for items that the State may not tax (e.g., United States government bonds). Another disadvantage is that the State would surrender its tax policy-making initiative to the federal government. In addition, State revenues would be dramatically affected by alterations in federal tax policy." *Id.* at 40.

VI. Conclusion

New York has the dubious distinction of having the highest average per-person income tax levy of any state in the country.[89] Equally disturbing is the fact that its rates are very uncompetitive with those of its neighboring states.[90] To add insult to injury, New Yorkers are even faced with excessive estate taxes upon death.[91]

On January 1, 1987, the State of New York will receive a tax windfall as a result of the enactment of the Reform Act.[92] This is an income tax windfall, and should be used solely to reduce the currently excessive New York income tax rates.[93] Moreover, the bias between investment income and earned income should be totally eliminated.[94]

The reduction in rates, however, must be substantial; otherwise, New York will accomplish no more than a freezing of its unenviably uncompetitive position in relation to other states.[95] If achieving a competitive position means lowering rates beyond the tax windfall, so be it.[96]

In the final analysis, taxpayers will look at the bottom line.[97] When so many acquaintances, colleagues and friends—with lifetime ties to New York—have already moved or retired elsewhere in order to escape New York's high income or estate taxes or both,[98] the time for endless study, debate and delay has passed. I trust, as in the past,[99] the New York Legislature will do its duty and move swiftly and meaningfully to aid the beleaguered New York taxpayer.

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89. *See supra* note 30 and accompanying text.

90. *See supra* notes 30-39 and accompanying text.

91. *See supra* notes 48-59 and accompanying text.

92. *See supra* notes 1-9 and accompanying text.

93. In 1985, approximately 59% of New York's revenue was derived from the income tax. *State and Local Taxes*, J. ACCOUNTANCY, Oct. 1986, at 31.

94. *See supra* notes 23-29 and accompanying text.

95. *See* Schmalz, *Revision Made In Cuomo Plan On State Taxes*, N.Y. Times, Dec. 11, 1986, at B1, col. 5; Goodman, *Cuomo's Insufficient Tax Cuts*, N.Y. Times, Dec. 10, 1986, at A31, col. 1.

96. *See First, Stop the Tax Windfall*, N.Y. Times, Dec. 12, 1986, at A34, col. 1. "Prudence dictates the quick fix, Cuomo-style. But New York does need a dramatic change in the tax system to break its image as a soak-the-rich state. The drive for major tax reform along the lines suggested by the Republicans should be postponed, not abandoned." *Id.* at A34, at col. 2.

97. *See Now Simplify the State Tax*, N.Y. Times, Sept. 29, 1986, at A14, col. 1.

98. *See* A. Lipman & W. Wisbaum, *Estate Planning For The Florida Bound New York Retiree*, N.Y. ST. B.J., Jan. 1978, at 26-29.

99. *See supra* notes 65-67 and accompanying text.