Tax Reform for Fairness Starts Here

News Analysis

by Bruce Fisher

How a lower sales tax can help Western New York

A scholarly conference held at Buffalo State College this past week brought distinguished historians from here and elsewhere together to discuss the political phenomenon of populism. Scholars mainly associate the term with William Jennings Bryan, who ran against William McKinley and gave voice to the frustrations of Midwestern farmers resentful of the bankers who made them poor. Journalist and commentator Rick Perlstein, author of *Nixonland* and of a forthcoming book about Reagan, noted that the Tea Party is the place Americans go today to express their anger at elites. But these days, populism is all about resenting the insiders and sophisticates and big guys, and not about economic fairness. Polls show that just about everybody in the USA knows full well that middle- and lower-income families have been squeezed and stressed and left behind over the past 30 years, while a slim sliver of the country has enjoyed fabulously disproportionate enrichment mainly through financial speculation. The Tea Party excoriates elites but embraces free-market fundamentalism in a Joe the Plumber version of the Ghost Dance movement: If we dance this dance, the good old days will reappear, and the invader from Hawaii, or Kenya, or Indonesia, will go away.

Awareness of something being terribly askew in the way the reward structure works today doesn't translate into economic populism. The reason? It might have been novelist John Steinbeck who said, "Socialism never took root in America because the poor see themselves not as an exploited proletariat but as temporarily embarrassed millionaires."

The other reason is that Democrats are reshaping themselves with the anti-ideology of Barack Obama—the intellectual who doesn't get angry, the leader who defines himself as a member of the cognitive elite, who hires Rahm Emmanuel, the genius who made $15 million being an investment banker in one calendar year based on his prowess as a fundraiser, a political insider, and a former ballet dancer, all on the square, right? Obama, who eschews confrontation and hires Larry Summers, the economist who, with Robert Rubin and other Goldman Sachs buddies, convinced Bill Clinton in 1999 to sign legislation that gutted 65-year-old regulations that had kept speculators in check and prevented financial bubbles. Oops. Obama, who, even after the bubble-pop, concedes the concerns of the financial elite rather than countering them. His "reforms" are tepid, squeamish, nonconfrontational, and have that Goldman Sachs air about them. To old-style economic populists, Obama is frustratingly consensus-oriented, and capitulates even before he's asked to. To those who pay close attention to issues of tax policy, securities regulation, and international trade rules, there is a clear pattern: Obama has joined the side of the speculators against the side of wage-earners, salary-earners, and pensioners.

The Tea Party is populist and complains about this elitism, but the Tea Party instead slams government support of the moderate- and low-income worker and retiree. Its populism is captive. Rewards for financial speculation continue to mount, and as the anti-regulatory lobbying of Wall Street succeeds in 2011 despite the Wall Street disaster of 2008, the relative economic and political power of the wage-earner, the salary-earner, the student, and the pensioner all fade—except insofar as the Tea Party in Congress guts their interests. The investor is now rewarded, and no more visibly than by the tax system.

And it's not just the national tax system. It's the state and local tax system, too.

Subsidizing mansion owners

In 2008, the latest year for which there are comprehensive figures, the median-income family in New York State paid more of its income in sales, income, property and excise taxes than the richest one percent. According to the Institute on Taxation and Economic Policy, if you make around $45,000 a year, which puts you in the middle of the middle class in New York State, you pay about 12 percent of your income in taxes. If you make over $630,000 a year, which puts you in the top one percent, you pay around seven percent of your income in taxes.

Now to local facts.

About two-thirds of Erie County households reported incomes of under $48,000 in 2008. It's the practice of most moderate-income families here and everywhere to spend all they make. Except for rent, food, and medicine, about 60 percent of the roughly $4,000 a month that a typical family here spends will be spent on items that are subject to sales tax. At almost nine percent, that $48,000 household is spending about $2,500 a year on sales tax.

But here's the rub: If most of the taxes that household is paying consists of taxes on consumption, then two facts are true. First, they're paying more than their share, and they're going to get hit harder and harder as the cost of energy goes up, because the largest chunks of money they're spending are for utilities and gasoline.

In most places in New York State, the basic state and local sales tax tops out at seven percent. For various reasons, Erie County has added an extra 1.75 percent. That's the part that Albany has to reauthorize.

Should Albany do so? Maybe. We've suggested that New York State should consider Erie County Executive Chris Collins's request to reauthorize 1.75 percent of the 8.75 percent sales tax, with a carve-out of a quarter penny to fund libraries, culturals, and the Convention and Visitors Bureau. The libraries should be funded because Collins is gutting a community cultural legacy that needs to survive him. The culturals should be funded because an investment of $6 million a year produces at least $240 million a year in economic activity, and it's just dumber than stupid to reduce economic activity here. The CVB actually does a good job of bringing outsiders in, and needs some sane support to do what the culturals: leverage local dollars to bring outside dollars in.

So New York State could leave the status quo in place, with the instruction that county government spend a quarter penny on the right stuff.

In the alternative, New York State could reauthorize the quarter penny for libraries, culturals, and tourism, and say no to the rest.

Why? One reason: fairness. Because that $48,000-a-year household is paying about $500 more than it should be paying in sales tax for stuff that should be paid for with property taxes.

The reason to advocate for a lower sales tax, even if the low-low-low county property tax rate has to be raised to make up the difference, is that the sales tax takes more from those who have less. The sales tax is a tax on consumption. It's the least fair way to collect revenue to buy public goods and provide public services. The fairest way to fund public goods is the income tax, but we're not about to see county-level income taxes created in New York State.

The high-income mansion-owner gets to itemize his deductions, and so reduces his tax hit. The owner of a median-value house doesn't itemize. And nobody gets a federal offset for local sales taxes. The mansion-owner and the real estate industry absolutely love the low property tax.

Erie County's low county property tax is an anomaly. Most county tax systems are set up with a sales tax of around seven percent, and a county-level property tax rate in the $10-$12-per-thousand range. (Property taxes are levied as a percentage of each $1,000 of assessed valuation.) Here in Erie County, the property tax rate is $5 per thousand, but the sales tax is almost nine percent. The theory of the higher sales tax was that everybody would pay—Canadians, drug lords, tourists, and over-the-road truckers—so as we increased the number of "transients" here, we'd make them pay for our local stuff. But the fact is that the largest payers of sales taxes are homegrown, and the biggest items subject to sales tax are utilities and cars and expenses related to cars. It's not fair to locals to have such a high sales tax just on the off chance that a few thousand visitors will chip in. And as for outsiders—masses of them shop at the Outlet Mall in Niagara County, where they pay less in sales tax than at the Galleria in Erie County.

Meanwhile, the county portion of the property tax here is nothing to scream about. Half the houses in Erie County are assessed at under $100,000—which means that the owners of half the houses here pay $40 a month or so in county property taxes. What would happen if their bills went from $40 to $70 a month? Answer: If their sales tax were cut from 8.75 percent to 7.25 percent, the majority of Erie County residents would make money. At least two-thirds of the families here would come out a few bucks ahead.

And that's how to bring home the issue about tax fairness: make Erie County a demonstration of the economic benefits to salary-earners, wage-earners, and pensioners of having a fairer tax system based on ability to pay, not based on dinging a consumer so that a mansion-owner gets a better deal.

Just to hammer the point home, consider the plight of a mansion-owner, and how it would actually not be such a bad trade-off for him, either. I know a guy who has a stupidly big house that is assessed at $300,000. The county property tax on this pig is $1,500 a year. If the county property tax went to $2,500 a year, he would scream—but he would still be able to deduct every penny of that $2,500 from his federal and state income taxes. Meanwhile, he would see his sales tax bill drop from almost nine percent to just over seven percent, and, as he spends a lot of money on utilities, his utility bill would drop noticeably. To make it drop more, would he now have even more of an incentive to insulate it and make it greener? Absolutely. And a lower sales tax rate might encourage him to buy a newer, greener car—because instead of paying almost $3,000 on a $30,000 car, he would pay $1,000 in sales tax on a new purchase.

What you're paying for

Then there's the equity question. Should we here, in the home of anti-tax radical Jack Kemp, not re-state the Rooseveltian idea that a richer guy should pay a larger share of the bill for public services than some person with a smaller house and a smaller income? Yes, of course we should. Will the rich guy squeal and whine about it? Yes, he will. Will he make out when Cuomo and Albany impose a property tax cap in 2011? Yes, he will.

And if the State Legislature reauthorizes only the quarter penny of sales tax and does so explicitly to save culturals, libraries, and the tourist bureau, he and everybody else in the community will not only benefit but they'll get a message. Perhaps they'll even understand better, as never before, that public funds do indeed enhance our quality of life. And then maybe, in the land that gave America the original Reagan Democrat, the Jack Kemp voter, we can begin the long political slog toward changing the Tea Party's protest energy into energy that actually benefits salary-earners, wage-earners, and pensioners rather than financial speculators. It starts with a campaign for tax fairness for sales-tax payers, and it should start here, and it should start now, in the year when Albany has a choice—a choice between either reimposing a massively regressive sales tax, or in getting some pro-consumer, pro-family equity back into the system.

Bruce Fisher is visiting professor of economics and finance at Buffalo State College, where he directs the Center for Economic and Policy Studies.