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A CASE STUDY IN FISCAL FEDERALISM: NEW YORK CITY AND NEW YORK STATE

Carol O'Cléireacáin*

Introduction

America's cities are in trouble. It is hard to find any that have not raised taxes and cut spending in order to balance their budgets in the past several years.¹ In part, of course, this crisis has resulted from a powerful national recession. Nonetheless, the American system of state and local government finance is seriously flawed and in need of repair. And in no place is that more obvious than New York City, which has a permanent structural imbalance between revenues and expenditures.

This essay argues that much of that imbalance has been imposed on New York City by other levels of government, and that only these forces can permanently repair the damage. New York State and New York City are currently groping toward such a solution with a radical proposal for a state takeover of Medicaid spending.

The first section of this essay discusses the fiscal relationship among America's levels of government and outlines the concept of "Fiscal Federalism." The second section presents the recent experience of America's cities, and particularly New York City, with Fiscal Federalism. The third section examines the issues involved in changing the fiscal relationship between New York State and New York City. Finally, the essay analyzes Governor Cuomo's proposal for a phased-in takeover of Medicaid spending and asserts that much more needs to be done to assist our nation's troubled cities in these times of federal retrenchment.

I. The American Federal Structure Today

The United States Constitution created a federal system of government where responsibilities not expressly designated to the central government belonged to the states.² The states subsequently de-

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¹. NATIONAL LEAGUE OF CITIES, CITY FISCAL CONDITIONS IN 1991 (July 1991). According to the National League of Cities, 85% of all U.S. cities either raised existing taxes or imposed new taxes in 1991. The percentage was even higher for Northeastern cities — 98%. Id. at iv.

². U.S. CONST. amend. X.
olved, through "home rule" arrangements, responsibilities to local
governments, such as counties, cities and school districts. As greater
flows of goods, services, people and money have tied the national
economy together, the fiscal arrangements among these levels of gov-
ernment have become both more complicated and less sensible.

For example, the growth of huge urban areas, which everywhere
cross county lines, and in the northeast, where they cross state lines,
mocks rational political and economic decision making. The principal
mechanism for county or city-suburban cooperation is state gov-
ernment, an entity disinterested, at worst, and slow, at best. Curren-
tly, the cities' and counties' power to tax is dependent upon the
states' authority. The only significant tax within the full authority of
local government is the property tax, and even that is levied under
state constitutional limitations and statutory controls, and is often
subject to taxpayer referenda.

Originally, local governments were charged with the responsibility
of providing basic services, such as police, fire, streets and water to
their resident population. Their focus was not to redistribute income
or wealth, nor to compensate for the deficiencies in health care,
schooling and training on a global or rural level. Yet, America's cities
have evolved as providers of services to areas well beyond their bor-
ders, and they continue to play a role in the national economy as we
approach the next century. This was no more evident than in 1989,
when the ten largest United States cities welcomed more than half of
America's immigrants.³

Cities also play a pivotal role in the nation's private economy,
where they provide work for millions (a large number of whom live
elsewhere), are the home to major employers and serve as the port of
entry for foreign goods and capital, as well as ports of exit for Ameri-
can services and tourists. That role is not reflected in either the distri-
bution of political power or the distribution of resources and
responsibilities of the public economy. This concentration is particu-
larly striking in light of the fact that fully one-third of Americans live
in cities.⁴

Through the years, ad hoc measures have evolved to recognize the
strains that urbanization has generated for the political institutions
created by a predominantly agrarian Constitutional convention in the

FISCAL FEDERALISM

18th century. Within the confines of the Tenth Amendment and the Interstate Commerce Clause, the federal government has, in this century, instituted a number of innovations which sought to better balance the fiscal flows with actual economic and political responsibilities.

One such measure was the introduction of a federal income tax to provide a basic mechanism for redistributing income from rich to poor. Both the tax’s progressivity and the responsiveness of its revenues to economic growth demonstrated, through time, that the federal government had a powerful tool, not only to repair some of the inequality of the private economy, but also to redistribute revenues within the public sector from the highest level of government to the lowest.

Economic theory supports the practical view that, with the broadest and most responsive tax base and an enforcement span from coast to coast, the national government is in the best position to tax and to provide public services. Despite this leverage on the part of the federal government, local taxes alone provide purely local services. Yet, with a highly mobile population, “purely local” is a shrinking concept. Beyond fire, sanitation and parks, it is not easy to find services which ultimately do not have “spillover” effects onto non-residents. The fact that Presidential candidates debate education policy, which is not a federally provided service, demonstrates that most Americans feel at risk if any locality is not properly educating its children.

While the political consensus may be to provide services at the local level, the economic consensus is that resources are raised most efficiently at the national level. By the early 1970s this arrangement of responsibility had become known as “Fiscal Federalism.” Accepting constitutionally designated political boundaries, economists set about rechanneling revenues in order to reach areas where problems were the most prevalent.

In the late 1960s, new federal spending created a range of specific local programs through specific grants. These grants ranged across several spectrums, including criminal justice, legal services, housing, community health and education. Nonetheless, this federal funding came with restrictions and tight controls. By contrast, during the

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Nixon and Ford Administrations, “Fiscal Federalism” became more general and less categorical in the form of major programs such as General Revenue Sharing8 (which had a special short-term anti-recession component during the mid-seventies) and the Comprehensive Employment and Training Act (“CETA”).9 Most of the money from these programs was used to maintain city services, or, ultimately, to substitute for local revenues.10

Ronald Reagan heralded his “New Federalism,” which was supposed to consolidate federal grants and free other levels of government from federally imposed constraints.11 This “New Federalism” virtually eliminated “Fiscal Federalism.” CETA was extinguished in 1982, although the actual death blow to this program was dealt during the Carter Administration. General Revenue Sharing finally died in 1987, after a long strangulation. While the hallmark of the “New Federalism” was the shift of enforcement responsibility to the states, the result has been simply fewer dollars without any alternative relief. Because Reagan’s “New Federalism” came at the same time as a massive cut in personal and business income taxes and a subsequent curtailment of their progressivity, the “revenue” in “revenue sharing” no longer existed. In effect, the substitution of the “New Federalism” for “Fiscal Federalism” moved state and local governments from revenue sharing to deficit sharing.

II. The Impact of Changing “Fiscal Federalism” on America’s Cities

According to the U.S. Conference of Mayors, federal aid to state and local governments fell by $34 billion in real terms during the 1980s.12 In addition, spending for key “urban” programs, such as community development, employment and mass transit fell by seventy-two percent between 1979 and 1989.13

13. Federal aid to state and local governments declined from $46.69 billion in FY80 (adjusted for inflation) to $13.14 in FY91. U.S. Conference of Mayors, The Federal Budget and the Cities, A Review of the President’s Budget for Fiscal
At the same time, federal taxes became less progressive. Following the federal income tax changes of 1986,14 which broadened the definition of income, and thus the tax base, states and cities with progressive income taxes adjusted their tax rates in order to avoid a "windfall" increase in revenues that would have resulted from the federal changes. It appears now that the "windfall" was grossly overestimated and/or never materialized. As a result, state and local tax revenues have suffered immensely.15 While these state and local governments were erroneously paring back their income taxes, their ability to raise sales taxes was seriously restricted by the elimination of federal deductibility. Also, their borrowing costs were raised through federal restrictions on the use of tax-exempt bonds.

Further, state and local governments bear the "mandate" burden on their tax bases alone. "Mandates" are the list of federal requirements, qualifications, prohibitions, specifications, constraints and controls on specific types of state and local spending. Originally, many of these mandates were attached to federal aid, and many remain attached by states to their localities. Their elimination would not directly impact the federal budget, but it would eliminate much uniformity.

In New York City, federal aid has been crucial over the past two decades. It was used during the city's fiscal crisis of the mid- to late 1970s to fund basic city services, including police and fire protection. By the time of Ronald Reagan's inauguration, when the federal commitment to state and local government had already peaked, one out of every five dollars New York City raised came from the federal government.

Ten years later, at the time of David Dinkins' inauguration as the city's first African-American Mayor, only one dollar out of ten that New York City raised came from the federal government.16 The cumulative loss of federal aid to New York City over the decade has been $25.2 billion.17 That, of course, was not the only change. During those ten years, the income of the top one percent of Americans

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rose nearly eighty percent, while the income of the poorest twenty percent of Americans fell by seven percent. The federal government's budget priorities shifted from spending seven dollars on the military for every dollar spent on housing to now spending twenty-seven dollars on the military for every dollar spent on housing.

New York City and New York State have worked to replace much, although not all, of the federal aid that was cut, with the city providing roughly two-thirds of the replaced funds. In the 1980s, the city's booming financial and real estate economy in addition to considerable borrowing made the replacement of federal revenues possible. In this current recession, that option has now ended.

Nonetheless, if the federal government were today providing the level of aid to New York City that it provided when Ronald Reagan took office, the city would have about $2.6 billion more revenue in this fiscal year. That is enough money to fund the entire police, housing, health, aging and youth services departments combined. The opportunity cost of the "New Federalism" in New York City is reflected in the rising infant mortality rate, overflowing hospital emergency rooms, seven month waiting lists for drug treatment and the doubling up of families throughout the public housing system.

This situation is not improving under the Bush Administration. Among other things, the 1990 federal budget agreement capped domestic spending for the next five years; set limits on the deductibility of all state and local taxes from federal taxes; encroached on traditional state and local revenue sources by raising tobacco and alcohol taxes; raised gasoline taxes while diverting some of those receipts from highways; and mandated social security payroll taxes for state and local government workers.

As the federal government remains hamstrung by its deficit reduction and budget agreement, all levels of government recognize this truth: while we have a multi-layered system, there is, ultimately, only one layer of taxpayers. If the federal government will not meet its responsibilities, there might be a "second-best" solution developing in New York.


III. Restructuring the Fiscal Relationship Between New York State and New York City

Because of its constitutional preeminence, New York State has the ultimate responsibility for ensuring the freedom, quality of life and a measure of justice for all of New York City's residents. The state exercises this responsibility in a number of ways — through the passage of laws, the operation of the courts, the regulation of commerce and industry, the raising and expenditure of public funds and the granting of taxing, spending and legislative authority to the city.

As a legal "creature" of the state, the city has a complex web of legal and fiscal relationships with the state. The state controls all city taxes, charging a fee to administer the income and sales taxes, and setting the rules for the property tax. The state provides funding for elementary and secondary education through a formula set each year. Much of city spending on education, criminal justice, health care and welfare services must meet state standards and is subject to fiscal penalties and sanctions if standards are violated. Aside from this political relationship, the state is strongly related to the city through the economy. Half of state tax revenues come from economic activity generated within the city; and forty percent of the state's jobs are located in the city.

These economic realities, as well as its constitutional responsibility, led the state to provide assistance to New York City during the fiscal crisis of the 1970s. The state took over a number of functions formerly funded by the city, such as the courts and senior colleges of the City University system. The state created a number of agencies to provide access to credit markets and financial oversight and assistance, such as the Municipal Assistance Corporation and the Financial Control Board.

Despite these new forms of assistance, New York State continues to impose fiscal burdens on the city that are imposed in very few other states. These burdens are imposed primarily on major redistributive programs. New York is one of only thirteen states that requires lo-

21. N.Y. Const. art. XVII, § 1. This section states, "The aid, care and support of the needy are public concerns and shall be provided by the state and by such of its subdivisions, and in such manner and by such means, as the legislature may . . . determine." Id.


yalities to pay a share of Medicaid costs and its fifty percent local share is far higher than that required by practically all of these states. The city's contribution to Medicaid costs were $1.6 billion in fiscal year ("FY") 91, a cost it would not have to bear if it were in any of thirty-seven other states. Further, New York is also one of only ten states that requires localities to pay a share of welfare costs, and once again, the fifty percent share is the highest of any state. This annual cost to New York City is $730 million.25

To fund these and other costs, New York State has granted New York City an unusual amount of local taxing power. As Figures 1 and 2 in Appendix A illustrate, the city has a budget of almost thirty billion dollars. Its tax revenues make it America's fourth largest taxing jurisdiction, larger than all states except California and New York. Not surprisingly, New York City's tax structure resembles that of states more than that of American cities.

New York State, on the other hand, has the lowest ratio of state taxes to local taxes of any state in America except for New Hampshire — only ninety-four cents for every dollar of local taxes.26 While New York State has a large budget, much of the state revenue is raised in New York City, including a number of taxes where more than seventy-five percent of the total revenue comes directly from activity in New York City.27

In the best economic and fiscal times, it is perhaps possible for a city like New York to accommodate the relatively high tax effort and spending levels necessitated by the state's fiscal policies. However, New York City is home to two-thirds of the state's poor people, and the local spending needs — public assistance, criminal justice, health care, special education — which this population generates are significant. Combined with the decade of reductions in federal aid discussed above and the prospects for little or no growth in the city economy, these fiscal burdens are no longer sustainable. The bulk of the projected gaps in New York City's budget now and into the future are due to these redistributive burdens. For example, in FY 1992, combined city Medicaid and income support costs of $2.3 billion plus the


27. Even in New York State's FY 1991, during a recession, New York City contributed $492 million (82 %) of the $597 million the state collected from the New York State Hotel Occupancy Tax, the Banking Corporation Tax and the Real Property Gains Tax. In boom years, these dollars were considerably greater.
1992 value of Reagan-era federal aid cuts of $2.6 billion exceeded the $3.5 billion FY 1992 budget gap by $1.4 billion.

This discrepancy came as no surprise. Since the 1960s when Medicaid and welfare programs were born, commissions have predicted that their burden would be unsustainable for New York City. In 1971, the New York City Commission on State-City Relations, chaired by William J. van den Heuvel, and comprised of future dignitaries such as Mario Cuomo, reviewed the work of previous task forces on New York City finances and concluded that the state's failure to assume these burdens was the primary cause of the city's chronic budget difficulties. The Commission noted:

New York State has too frequently acted like a philanthropic foundation rather than a state. The State has failed to assume the responsibility which its own sovereignty implies and has proven unwilling to confront problems which it, through its constitutional powers of taxation, has the fiscal capacity to solve. . . .

Now, however, a change is in the works. A bold new idea has been proposed by now Governor Mario Cuomo. In this plan, Governor Cuomo seeks to relieve New York City of some of its financial and service burdens in order to allow it to achieve a new and necessary degree of financial stability.

IV. Fiscal Federalism in New York State and Governor Cuomo's Medicaid Takeover Proposal

The size of the burdens borne by New York City raise serious questions about whether the current fiscal relationship is economically sustainable for both the city and state, and whether the relationship is consistent with the duty of the state to provide equal protection to all of its citizens, which is the goal of a fair and just society. The obvious questions raised by the present relationship are:

1. What mix of spending and taxing authority is most consistent with the state's constitutional responsibilities and the economic interests of both the state and city?
2. What are the economic and social consequences of the existing fiscal relationship?
3. Are there state spending requirements which should be reduced or eliminated and how should such reductions be financed?
4. What are the constitutional, legal and political changes neces-

29. Id. at 31.
sary in order to restructure the fiscal relationship between the state and city?

(5) What is a realistic timetable to make this happen?

Since May 1991, both New York City and New York State have been trying to answer these questions and fashion a workable new "Fiscal Federalism". The result tells us much about how politics shapes attempts to restructure fiscal relationships.

A. The Medicaid Takeover Proposal

In September 1991, Governor Cuomo announced a proposal for a phased takeover of local Medicaid costs, stating:

[I]n one bold step, we can dramatically improve the affordability of quality public health care and relieve local governments and property taxpayers of the most significant burden imposed upon them by the State of New York. 30

Table 1 provides a capsule summary of the Governor's complex proposal for an eight-year phased-in state take over of Medicaid spending from localities. The Governor has proposed several stages in the take-over:


(1) The state implements a series of "cost containment" measures leading to state and local savings and bringing down the growth rate of Medicaid spending in later years.
(2) The state also examines how and when it will take over the administration of Medicaid.

2. Stage Two: SFY 1993-1997

(1) The state picks up a larger share of the costs of Medicaid recipients enrolled in managed care (i.e. HMO-type) programs. 31
(2) In SFY 1995 the state picks up one hundred percent of local administrative costs of Medicaid. 32


31. Current state law already requires local governments to enroll up to half of all their Medicaid eligibles by 1997. This part of the proposal is clearly meant to provide the financial incentive for localities to meet this recently mandated requirement.

32. See GOVERNOR'S RELIEF PROPOSAL, supra note 30, at Table 4. Administrative costs are estimated to represent approximately 2.7% of total costs in SFY 1993.
3. *Stage Three: SFY 1997-2000*

(1) The state incrementally assumes the remaining local share of Medicaid spending.

To help the state pay for the takeover, New York City incrementally gives up its personal income tax revenues, beginning at seventy-five percent in SFY 1997 and culminating in one hundred percent in SFY 2000. Other localities give up .85 percentage points of their sales tax rate in SFY 1998 and a full percentage point in and after SFY 1999.

**Table 1**  
**Summary of the Governor's State Assumption Plan**

<table>
<thead>
<tr>
<th>SFY</th>
<th>Cost Containment as a percent of Total Expenditures(a)</th>
<th>Percent Assumption of Local Administration(b)</th>
<th>Percent Assumption of Managed Care</th>
<th>Percent Assumption of Local Revenues</th>
<th>Percent Assumption of Remaining Expenditures</th>
</tr>
</thead>
<tbody>
<tr>
<td>1993</td>
<td>2%</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>1994</td>
<td>4%</td>
<td>—</td>
<td>50%</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>1995</td>
<td>4%</td>
<td>100%</td>
<td>70%</td>
<td>75%</td>
<td>0.85 pt (c) 80%</td>
</tr>
<tr>
<td>1996</td>
<td>4%</td>
<td>100%</td>
<td>70%</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>1997</td>
<td>4%</td>
<td>100%</td>
<td>100%</td>
<td>75%</td>
<td>0.85 pt (c) 80%</td>
</tr>
<tr>
<td>1998</td>
<td>4%</td>
<td>100%</td>
<td>100%</td>
<td>80%</td>
<td>0.85 pt (c) 80%</td>
</tr>
<tr>
<td>1999</td>
<td>4%</td>
<td>100%</td>
<td>100%</td>
<td>90%</td>
<td>1.00 pt (c) 90%</td>
</tr>
<tr>
<td>2000</td>
<td>4%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>1.00 pt (c) 100%</td>
</tr>
</tbody>
</table>

Notes:  
(a) Percentages are approximate. State plan is not based on precise 4 percent reduction. The $150 million cost containment program in fiscal year 1994 averages approximately 4 percent in that year and in all subsequent years.  
(b) Administration of managed care would remain with localities until after fiscal year 2000.  
(c) pt designates percentage point.


Table 2 summarizes the state's estimates of the total savings to localities under the Governor's plan: more than $5 billion over eight years. Annual savings by the year 2000 are estimated to be in excess of $1.6 billion.
### Table 2
**Financial Gain to Localities Under Governor's Medicaid Takeover Plan**
($ Millions)

<table>
<thead>
<tr>
<th>SFY</th>
<th>Total Savings Less From Takeover and Cost Cutting</th>
<th>Less Revenue Net Gain To SFY and Cost Cutting Swap Localities</th>
</tr>
</thead>
<tbody>
<tr>
<td>1993</td>
<td>$ 82</td>
<td>$ 82</td>
</tr>
<tr>
<td>1994</td>
<td>202</td>
<td>202</td>
</tr>
<tr>
<td>1995</td>
<td>365</td>
<td>365</td>
</tr>
<tr>
<td>1996</td>
<td>486</td>
<td>486</td>
</tr>
<tr>
<td>1997</td>
<td>4,086</td>
<td>$3,556</td>
</tr>
<tr>
<td>1998</td>
<td>4,671</td>
<td>3,973</td>
</tr>
<tr>
<td>1999</td>
<td>5,770</td>
<td>4,732</td>
</tr>
<tr>
<td>2000</td>
<td>7,039</td>
<td>5,434</td>
</tr>
</tbody>
</table>


Localities save in two ways under this plan. First, in the short- to mid-term, they derive the benefits of Medicaid cost containment as quickly as it can be realized, and only so long as they continue to bear a share of spending. Second, in the longer run they save the net difference between Medicaid spending and tax revenues. By giving up revenues that grow more slowly than Medicaid, local governments lose the major source of their present and future deficits. The value of the savings equals the dollar difference between the revenue and Medicaid growth rates.33

While all counties would benefit, as Table 3 shows, New York City receives the bulk of the savings. This is the result of the fact that the city is home to two-thirds of the state’s Medicaid eligibles. The state estimates that New York City will save approximately $3.25 billion by SFY 2000 and $1 billion annually once the program is fully phased in.

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33. The state estimates a Medicaid growth rate of approximately 12% annually, while in most cases the local tax revenues being given over to the state are estimated to grow at 5-6 % annually.
Table 3
Net Financial Gain to New York City and Other Counties
($ Millions)

<table>
<thead>
<tr>
<th>SFY</th>
<th>NYC</th>
<th>Counties</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>1993</td>
<td>$ 57</td>
<td>$ 25</td>
<td>$ 82</td>
</tr>
<tr>
<td>1994</td>
<td>142</td>
<td>60</td>
<td>202</td>
</tr>
<tr>
<td>1995</td>
<td>252</td>
<td>113</td>
<td>365</td>
</tr>
<tr>
<td>1996</td>
<td>336</td>
<td>150</td>
<td>486</td>
</tr>
<tr>
<td>1997</td>
<td>336</td>
<td>194</td>
<td>530</td>
</tr>
<tr>
<td>1998</td>
<td>424</td>
<td>274</td>
<td>698</td>
</tr>
<tr>
<td>1999</td>
<td>678</td>
<td>360</td>
<td>1,038</td>
</tr>
<tr>
<td>2000</td>
<td>1,037</td>
<td>568</td>
<td>1,605</td>
</tr>
</tbody>
</table>


B. Analysis of the Takeover Plan

Stages I and II of the Governor's proposal — cost containment and managed care — raise a number of health policy questions, such as how to cut costs without drastically reducing access to care and whether there will be enough primary care physicians for the managed care program. The administrative takeover proposal raises questions regarding the impact on local Medicaid workers and the ability of the state to run a program it has never run before. While these are major public policy issues, they are not the focus of this essay and will not be addressed here.

The key question here is to what extent does the Governor's proposal represent "Fiscal Federalism": funding the costs of redistribution from the rich to the poor through the widest, broadest and fairest tax base possible?

Unfortunately, the answer is "not very much."

Currently, New York City pays about seventy-four percent of local Medicaid costs in New York State. Since city residents pay about thirty-five percent of state taxes, the city could be expected to pay approximately thirty-five percent of Medicaid costs if they were financed statewide. The Governor's plan would shift approximately twenty percent of the city's Medicaid costs to the statewide tax base, dropping the share of local Medicaid costs paid by city residents to roughly sixty percent, still way above the thirty-five percent
benchmark.34

"Fiscal Federalism" involves more than economics; politics are crucial to making it happen. As such, there are special political problems involved in a state takeover of Medicaid and/or welfare.35 These are major redistributive programs and, therefore, any shift to the statewide tax base carries important distributional consequences. Many parts of the state, particularly wealthy suburban counties, pay less than their fair share of Medicaid costs. They have done so since the beginning of these programs and, until now, had expected to continue to do so. Since city representatives account for only forty percent of both houses of the state legislature, any proposal for a state takeover must be crafted to win support from legislators elected from other areas.

The Governor made the political assumptions underlying his proposal clear when he released it. He acknowledged that "the reality of the state's fiscal condition makes a simple takeover of Medicaid impossible without either inordinately increasing taxes or imposing overwhelming cuts in other programs."36 Given the unattractiveness of either option, Governor Cuomo's fiscal imperative became using the local tax base to pay for the bulk of the program and employing cost containment as both a financing source and a political carrot to Republicans in both houses.

Can the state not "afford" a takeover? The answer depends on how one defines the "state." The Governor defines it as the existing budget of the State of New York; and with a looming $4 billion budget gap, the state budget cannot easily accommodate nearly $3 billion of new spending. However, if one defines the "state" as the sum of all of its governments, local jurisdictions included, the answer is that it is not unaffordable. Viewed from this perspective, a takeover is not solely a budget issue. It is an issue of redistributing spending and taxing burdens with no net enlarging of the size of New York State's public sector.

Let me illustrate how this could work.

34. Roistacher, supra note 25, at 26, 28. See also Governor's Relief Proposal, supra note 30, at Tables 1, 4.
35. Welfare programs in New York and most other states are designed to supplement the incomes of (usually) very poor households. These supplements are either unrestricted cash grants or payments for specific goods, such as food, heating or shelter. The major welfare programs in New York are Aid to Families with Children (New York State's version of the federally-mandated Aid to Families with Dependent Children program), Food Stamps (which is 100% federally funded), Home Relief and the Low Income Home Energy Assistance Program.
In May and November of 1991 the Citizen's Budget Commission proposed a "tax swap" where the state would take over both local Medicaid and welfare costs, paid for by an increase in the state Personal Income Tax ("PIT"). In exchange, localities would cut their own (property or sales) taxes by an amount equal to their savings. Total Medicaid and welfare spending would not increase; nor would total taxes collected statewide. But the distribution of these burdens around the state would change dramatically. Residents of counties with high incomes and small poverty populations would pay more; residents of counties with the opposite characteristics would pay less.

In a Medicaid-only takeover, analysts estimate that "winner" counties (those whose local tax cuts would be greater than their additional state PIT payments) account for only forty-four percent of the state population, nearly all of which is New York City. Unfortunately, it is hard to imagine enough votes for a winning coalition in the State Legislature for such a solution.

But, if there are enough "winner" counties — where the Medicaid and/or welfare spending exceeds the share of net new taxes they would have to bear from a tax swap — to generate a majority of legislators, then we can assume that "Fiscal Federalism" is politically feasible in New York.

This author constructed a number of takeover scenarios to test them against this standard. And, as Table 4 demonstrates, it is possible to develop a takeover proposal that could be passed by the State Legislature and also satisfy our definition of "Fiscal Federalism", i.e. effective redistribution. Table 4 contains five scenarios where the state takes over either Medicaid or public assistance, at varying takeover percentages, and does not have to raise the state income tax rates above the levels of the mid-1980s.

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38. Roistacher, supra note 25, at 20.
39. Id.
40. Since the state has embarked on a sequence of personal income tax cuts, raising the state tax is an important issue.
### Table 4
Medicaid and Public Assistance
Takeover Options (1991)
($ billions)

<table>
<thead>
<tr>
<th>State Takeover Option</th>
<th>Cost/(Savings)</th>
<th>NYS Counties Benefitting(b)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>State</td>
<td>NYC</td>
</tr>
<tr>
<td>100% Medicaid</td>
<td>$3.6</td>
<td>$(2.5)</td>
</tr>
<tr>
<td>100% Public Assistance</td>
<td>$2.5</td>
<td>$(1.8)</td>
</tr>
<tr>
<td>50% Medicaid in NYC,</td>
<td>$2.7</td>
<td>$(1.6)</td>
</tr>
<tr>
<td>100% Medicaid in other</td>
<td></td>
<td></td>
</tr>
<tr>
<td>counties, 100% Public</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Assistance, all counties</td>
<td></td>
<td></td>
</tr>
<tr>
<td>25% Medicaid in NYC,</td>
<td>$2.2</td>
<td>$(1.1)</td>
</tr>
<tr>
<td>100% Medicaid in other</td>
<td></td>
<td></td>
</tr>
<tr>
<td>counties, 100% Public</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Assistance, all counties</td>
<td></td>
<td></td>
</tr>
<tr>
<td>100% Public Assistance,</td>
<td>$1.1</td>
<td>$(0.7)</td>
</tr>
<tr>
<td>all counties</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Notes:  
(a) The current top PIT rate is 7.875%.  
(b) A county is defined as benefitting if its savings from the takeover exceed additional state PIT payments made by its residents.

A full takeover of Medicaid and welfare appears not to be a political winner, since it would benefit only seventeen of the state's fifty-seven counties. However, a state pick-up of twenty-five percent of New York City Medicaid costs and one-hundred percent of the Medicaid costs of other counties, as well as a full takeover of public assistance costs, would benefit thirty-six of fifty-seven counties — a substantial majority. New York City would still save more than $1.1 billion. If the city chose to reduce its own PIT by the amount that city residents pay for the additional state income tax burden ($770 million), i.e., hold city residents harmless for the tax increase, there would still be a net New York City budget savings of $330 million. In this scenario, the top state income tax rate would be nine percent — higher than the present rate of 7.875 percent, but lower than California's ten percent rate and lower than the top state rate in effect as recently as 1986.
V. Conclusion

The thesis of this paper has been that only a thorough restructuring of "Fiscal Federalism" can yield the kind of budgetary relief that will allow New York City to improve services or reduce taxes, and that in doing so our state and nation will be better off. Unfortunately, the present distribution of taxation and spending in New York State creates a calculus of "winners and losers" which must be addressed. The legacy of inadequate "Fiscal Federalism" in New York State works as a huge barrier to the creation of a more rational and equitable sharing of fiscal burdens. The time has come to address that legacy and the unfair burden it has created. Governor Cuomo’s Medicaid takeover proposal is a step in the right direction. However, more can be done. New York State must work together with New York City to fashion a bold new approach to allow "Fiscal Federalism" to became an effective and efficient reality.
Figure 1
NYC REVENUES
FY 1992 FORECAST
TOTAL: $28,661 MILLION

Figure 2
NYC TAX COLLECTIONS
FY 1992 FORECAST

TOTAL: $16,879 MILLION

PROPERTY 46%
$7,824

PERSONAL INCOME 18%
$3,086

SALES 14%
$2,410

BUSINESS INCOME 11%
$1,808

COMMERCIAL RENT 4%
$750

OTHER 6%
$1,021
