Forecasting Challenges in Light of Tax Policy Changes

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Forecasting Challenges in Light of the Tax Cuts and Jobs act.

✓ Interpreting the law

✓ Addressing the State and Local tax policy legislative issues, conformity, and work around.

• Determining short-term intertemporal behavior compared to long-term structural changes.

• Incorporating new information into existing econometric models

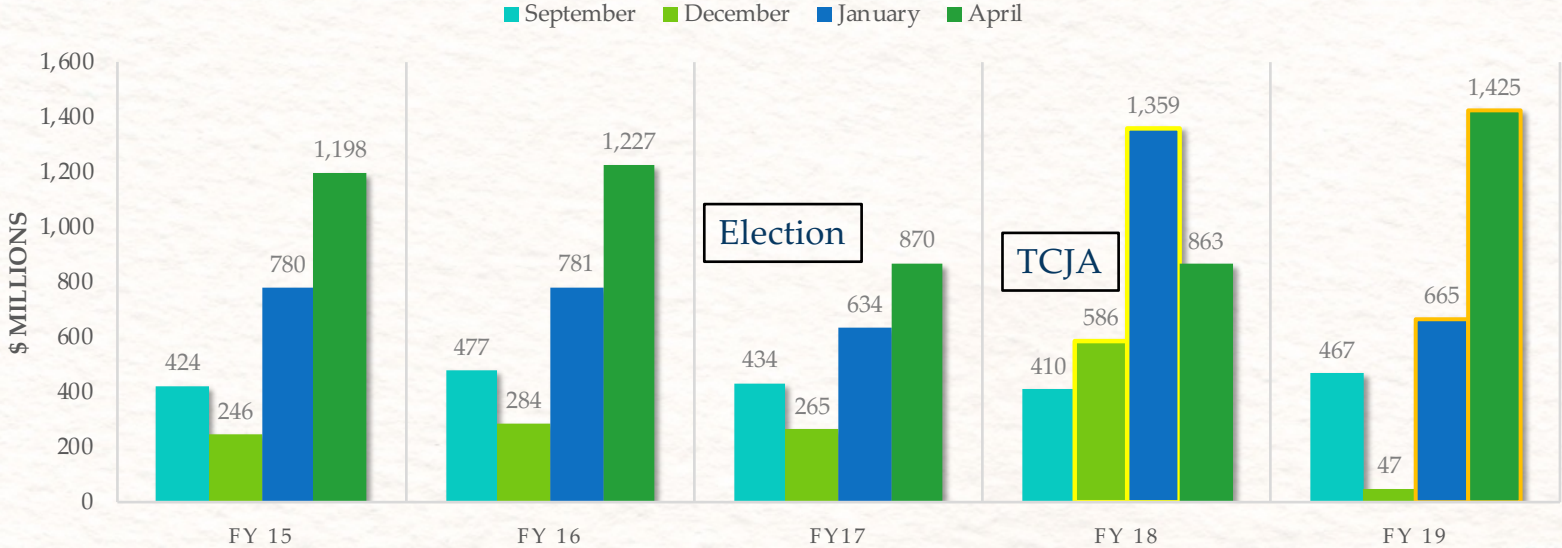| Intertemporal	Structural
• Typically one time in nature • Behavioral • Shifting income/liability from one period to another to minimize tax liability • Example: In order to take advantage of uncapped State & Local Tax (SALT) deductions, individuals maximized State and Local tax liability at the end of 2017.	• Permanent • Economic • Example: Capping SALT makes high tax (income and property) jurisdictions less competitive. – Less State & Local income liability

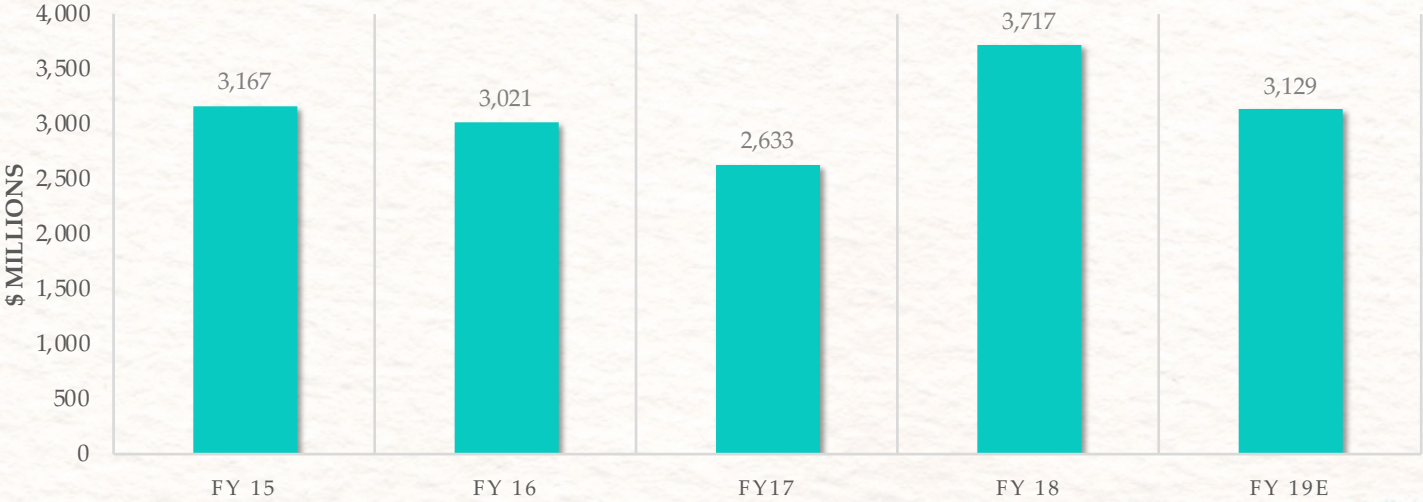# Challenges Introduced by Intertemporal Shifting

Challenge: Intertemporal shifting complicates forecasting.

NYC INSTALLMENT/ESTIMATED PAYMENTS

■ September   ■ December   ■ January   ■ April

$ MILLIONS

	September	December	January	April
FY 15	424	246	780	1,198
FY 16	477	284	781	1,227
FY17	434	265	634	870
FY 18	410	586	1,359	863
FY 19	467	47	665	1,425

Election

TCJA

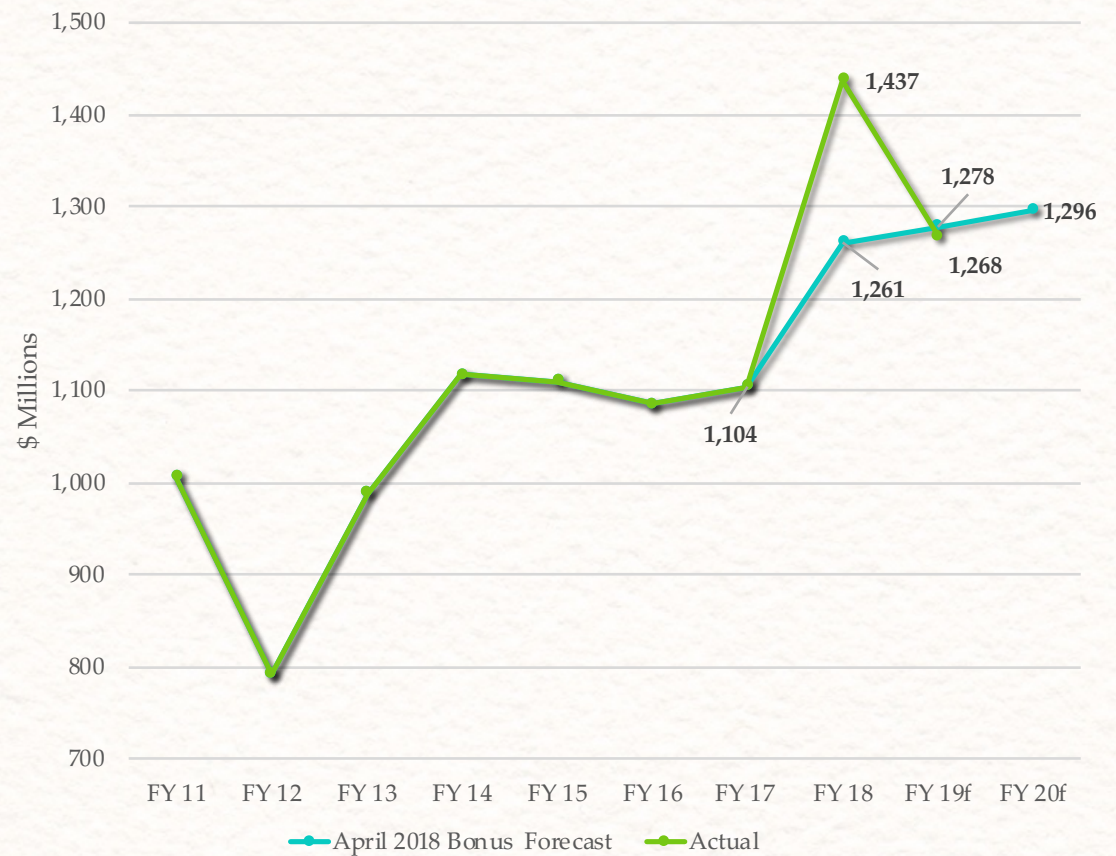# *Challenge: Determining one-time behavior*

NYC INSTALLMENT/ESTIMATED PAYMENTS

Challenge:
Forecasting bonus payments subject to a one time exogenous shock

April 2018

Economic forecast underestimated one time bonus revenue from TCJA and NQDC in FY 2018, but forecast FY 2019 accurately

$ Millions

1,437
1,278
1,296
1,261
1,268
1,104

FY 11 FY 12 FY 13 FY 14 FY 15 FY 16 FY 17 FY 18 FY 19f FY 20f

April 2018 Bonus Forecast   Actual

Structural Challenges

How does the SALT CAP impact NYC's long run income tax forecast?

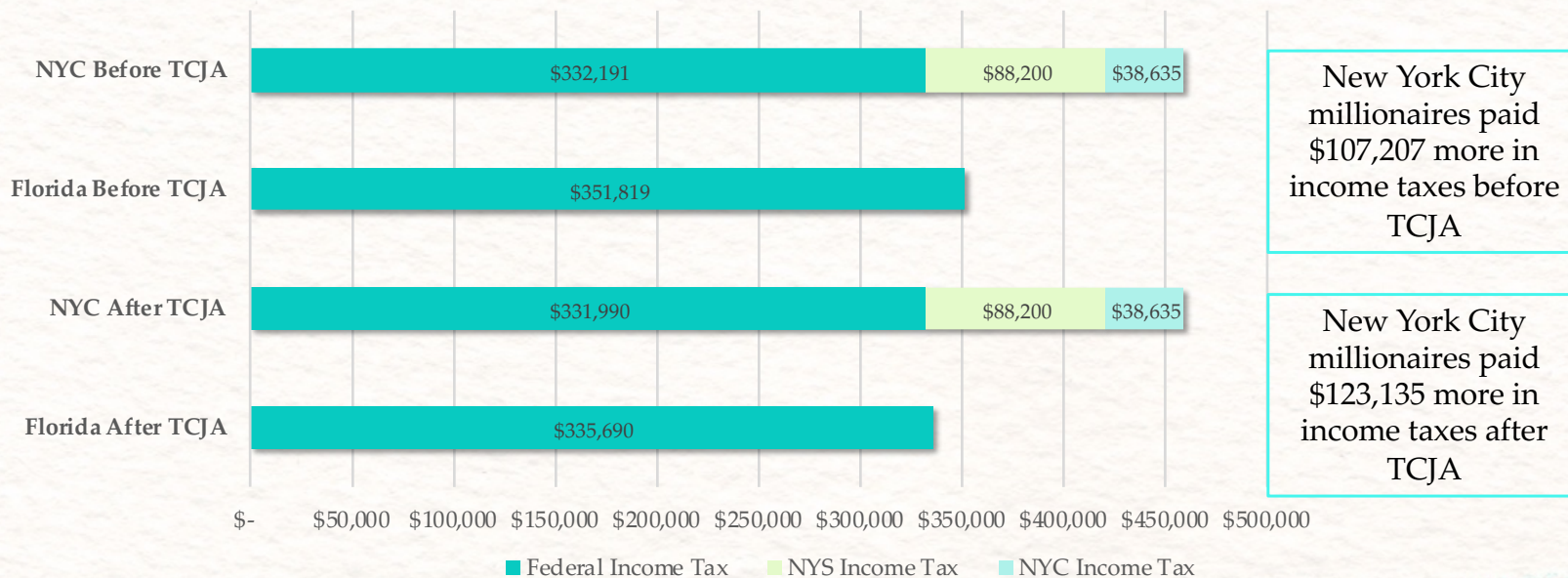*Challenge*: Who is impacted by the cap on SALT deductions?

NYC has a relatively high State & Local income tax burden.

State	Top Tax Rate
California	13.3%
NYC & NYS	12.696%
Hawaii	11.0%
New Jersey	10.75%
Oregon	9.90%
Minnesota	9.85%

- **NYC residents took $34 billion in State & Local tax deductions in 2016. (SOI)**

Challenge: High income "millionaires" filers face the greatest impact from the SALT deduction cap. However, NYC residents were already facing higher income tax burdens than low tax/no tax locales.

Filer with $1m in Taxable Income Before SALT deduction

	Federal Income Tax	NYS Income Tax	NYC Income Tax
NYC Before TCJA	$332,191	$88,200	$38,635
Florida Before TCJA	$351,819		
NYC After TCJA	$331,990	$88,200	$38,635
Florida After TCJA	$335,690		

New York City millionaires paid $107,207 more in income taxes before TCJA

New York City millionaires paid $123,135 more in income taxes after TCJA

$- $50,000 $100,000 $150,000 $200,000 $250,000 $300,000 $350,000 $400,000 $450,000 $500,000

■ Federal Income Tax   ■ NYS Income Tax   ■ NYC Income Tax

Challenge:

Historical evidence, NYC "millionaires" and NYS top tax rate

NYS Top Rate

8.970%

6.850%
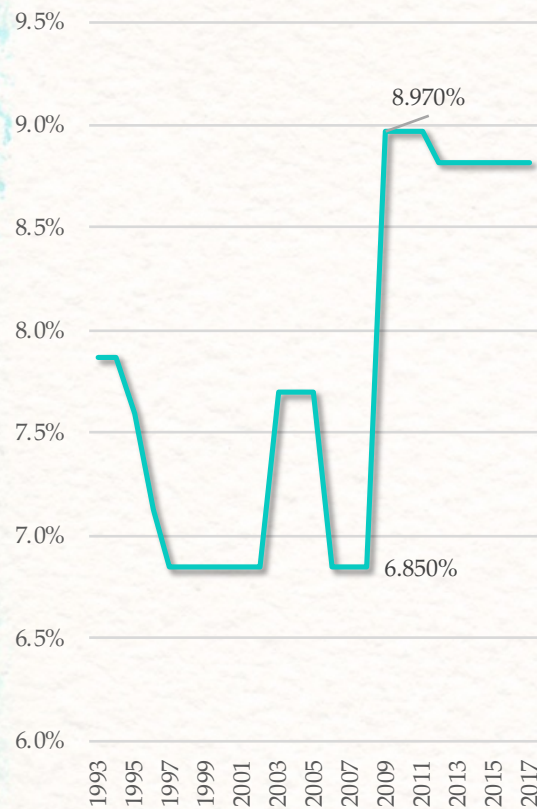
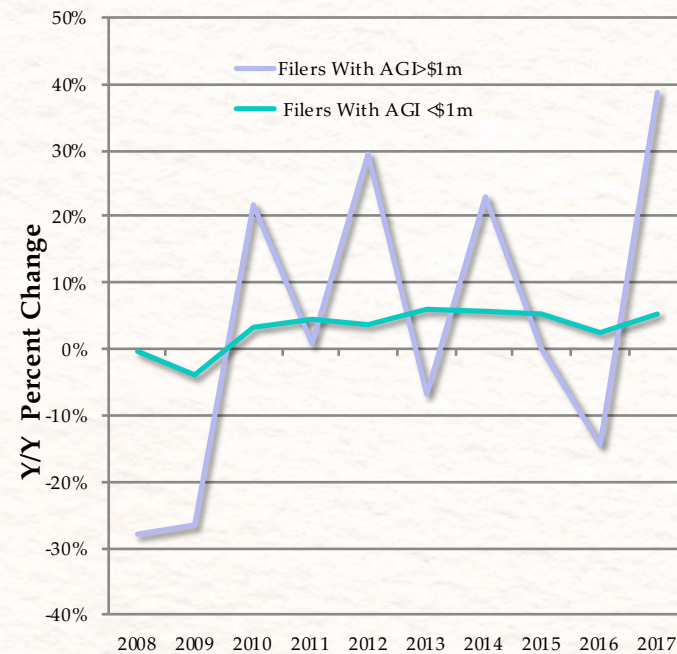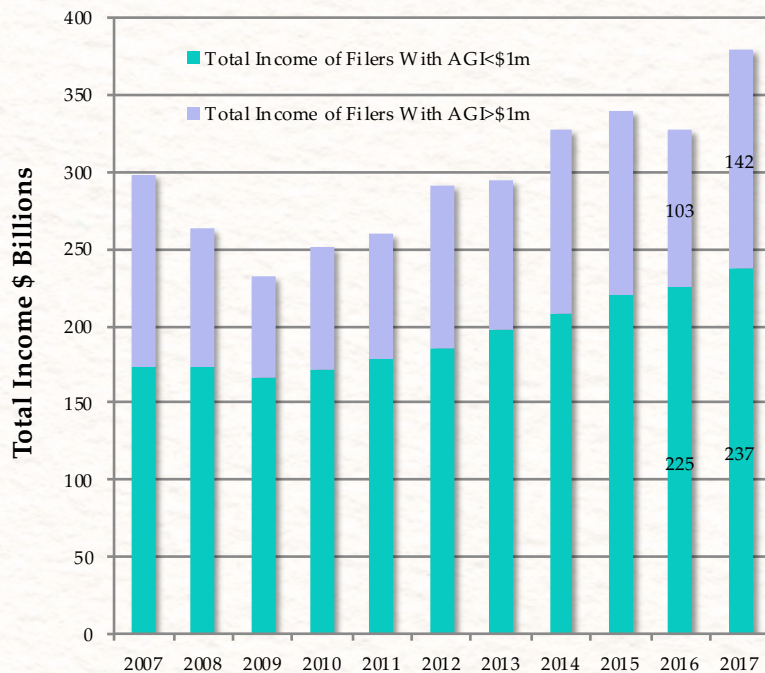### Number of NYC Filers with AGI > $1m
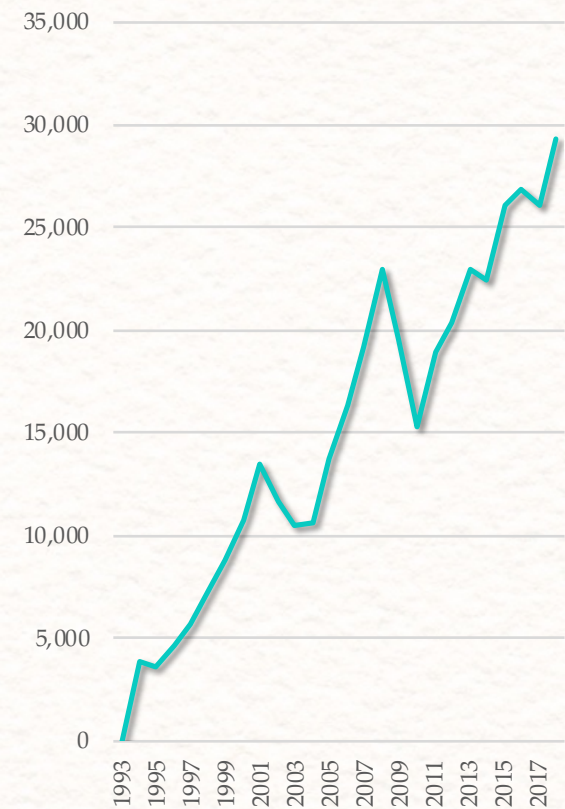
Challenge: NYC has about 30k filers with AGI > $1m. They account for over 1/3 of the AGI. Their income has always been volatile.

Summary of Challenges

1. Determine what is intertemporal and what is structural

2. Control for the intertemporal behavior
   - Forecast based on economic fundamentals, might help explain magnitude of one time nature.
   - Incorporate dummy variables to avoid future bias

3. Address structural changes
   - Determine who is impacted by policy change
   - Determine impact of policy change
   - If possible, incorporate information into models: add national/local tax rates into equations.
   - Careful not to double count the impact if independent variables already show behavior.

Other questions

- Does the SALT CAP make NYC relatively less competitive, reducing income recognized in NYC?

- Does the SALT CAP reduce demand for housing resulting in lower prices, fewer transactions, and ultimately lower property taxes.

- Do lower corporate tax rates increase capital gains (buy backs) or dividend payments?

- Do C-corps convert to pass-throughs or do pass-throughs convert to C-Corps?

- Does the introduction of Opportunity Zones impact capital gains?
  – Deferral might reduce short-term capital gains, but might not differ from section 1031
  – Step-up basis might reduce long term capital gains income.