LEGISLATIVE FISCAL ESTIMATE

[First Reprint]

SENATE, No. 1562

STATE OF NEW JERSEY
215th LEGISLATURE

DATED: AUGUST 3, 2012

SUMMARY

Synopsis: Increases amount of tax credits authorized to be issued under Urban Transit Hub Tax Credit program and extends application deadline.

Type of Impact: Unknown net effect of three countervailing impacts: 1) a recurring revenue loss to the State General Fund and the Property Tax Relief Fund from awarding tax credits; 2) a recurring revenue increase to the State General Fund, Property Tax Relief Fund, and local governments from receipts catalyzed by credit-induced economic activity; 3) recurring opportunity costs to State from granting credits.

Agencies Affected: Department of the Treasury.
New Jersey Economic Development Authority.
Local Governments.

Office of Legislative Services Estimate

Fiscal Impact	FY 2013 and 2014	FY 2015 through 2028	FY 2029
Direct State Revenue Loss	$0	Up to $250,000,000	$0
State Opportunity Cost	Indeterminate — See comments below		
Indirect State Revenue Gain	Indeterminate — See comments below		
Indirect Local Revenue Gain	Indeterminate — See comments below		

- The Office of Legislative Services (OLS) can project neither the direction nor the magnitude of the bill's net fiscal impact on the State and local governments.

- On the one side of the ledger, the OLS estimates that the bill will produce a total State revenue loss of up to $250 million through FY 2028 from awarding additional Urban Transit Hub tax credits plus their indeterminate opportunity costs—opportunity costs capture the fiscal benefits the State forgoes as spending is redirected from one economic activity to another. The estimated $250 million maximum State revenue loss through FY 2028 reflects the difference between the tax credit program's current $1.5 billion cap and the bill's revised $1.75 billion cap. The New Jersey Economic Development Authority (EDA) has awarded

$977.1 million in urban transit hub tax credits to 18 projects through June 13, 2012.

- On the other side of the ledger, additional tax credits that are essential to the realization of capital projects in designated areas will also generate indirect fiscal benefits to the State and local governments that may, or may not, exceed the cost and opportunity cost of providing the financial assistance. The OLS, however, cannot gauge the number, type, and scale of tax credit-induced capital projects and their ensuing indirect effects on State and local government tax receipts.

- The indirect fiscal effects from capital projects that would be undertaken with or without the tax credit have to be excluded from the analysis. This is so because whenever the tax credit has no bearing on the decision to carry out a project, it merely produces sunk costs to the State, or an expense without a benefit. Applying this general principle to this bill, it is reasonable to expect that most of the tax credits' indirect effects will count as a benefit. This is so because credits can only be awarded if a project passes the net benefit test. As part of that test, the EDA excludes from the analysis the indirect benefits from jobs that are neither "at risk" nor classified as a "suburban to urban move" nor otherwise deemed new jobs to the State. Therefore, only those tax credits will not produce an indirect revenue gain to the State that represent a relocation of jobs from a suburban area of the State to an urban area or that represent an incorrect assessment regarding the likelihood of a job created or retained within New Jersey absent a credit award. It remains unclear, however, whether or not the indirect revenue gains attributable to the credits will exceed the direct State revenue loss and opportunity cost they will cause.

BILL DESCRIPTION

Senate Bill No. 1562 (1R) of 2012 raises the total lifetime cap on the urban transit hub tax credit program by $250 million from $1.5 billion to $1.75 billion and extends the deadline for initial tax credit application submissions from January 13, 2013 to July 1, 2014 and for final tax credit application submissions from January 12, 2016 to July 28, 2017.

Under the program the State awards tax credits to taxpayers who make eligible capital investments in real property in urban transit hubs. Urban transit hubs are the area within a one-half mile radius around a rail or light rail station in Camden, East Orange, Elizabeth, Hoboken, Jersey City, Newark, New Brunswick, Paterson, and Trenton, with the Camden urban transit hub covering the area within a one-mile radius around a rail or light rail station. In addition, there is an urban transit hub in the area within a one-mile radius of a rail or light rail station that is subject to a Choice Neighborhoods Transformation Plan. (The only New Jersey Choice Neighborhood is currently in Jersey City at the McGinley Square – Montgomery Corridor.) Acute care medical facilities and closed hospitals located within a one-mile radius of a rail or light rail station also qualify for tax credits.

To qualify for a business facility tax credit of up to 100 percent of the investment under the urban transit hub tax credit program, a capital investment in real property must: a) equal at least $50 million; b) pave the way for at least 250 full-time employees working in the business facility; c) be made by July 28, 2017 under the bill; and, d) under most circumstances, yield a net positive benefit to the State and the municipality hosting the transit hub.

Tenants in qualified business facilities may also receive a credit if they occupy space in the facility that represents at least $17.5 million of the capital investment and employ at least 250 persons in the facility. If fewer than 200 of the 250 full-time positions in a business facility represent a net gain to New Jersey, then the tax credit maxes out at 80 percent of the qualified capital investment.

To qualify for a residential tax credit of up to 35 percent of the investment, an investment in a residential project must: a) equal at least $50 million; b) be made by July 28, 2017 under the bill; and c) not occur absent the receipt of a tax credit.

Two mutually exclusive tax credit options exist for developers of mixed use projects representing a capital investment of at least $50 million. They may either receive a residential tax credit for the entire investment subject to the conditions of that tax credit or they may receive a residential tax credit for the project's residential component if it represents at least a $17.5 million capital investment and otherwise meets the conditions of that tax credit and a business facility tax credit for the project's business facility component if it represents at least a $17.5 million capital investment and otherwise meets the conditions of that tax credit.

FISCAL ANALYSIS

EXECUTIVE BRANCH

None received.

OFFICE OF LEGISLATIVE SERVICES

The OLS can determine neither the direction nor the magnitude of the net fiscal impact on the State and affected local governments of the bill's increase in the urban transit hub tax credit program cap and its extension of the program's initial and final tax credit application submission deadlines. In general, the State net fiscal impact is calculated by adding the direct revenue loss from granting additional tax credits and their opportunity costs (the fiscal benefits the State forgoes as spending is redirected from one economic activity to another) and subtracting from that sum the indirect revenue gain from granting the tax credits. In addition, the bill is also likely to accrue an indirect revenue gain to local governments.

Although the OLS is able to pinpoint the bill's maximum direct revenue loss, it cannot calculate its opportunity cost or its offsetting indirect revenue gain. This inability is rooted in the dearth of reliable information on the characteristics of capital investments that will earn tax credits.

Direct Fiscal Impact: The bill's direct revenue loss to the State General Fund and Property Tax Relief Fund from raising the urban transit hub tax credit program cap and extending the program's initial and final tax credit application submission deadlines could be as high as $250 million accumulated over several years, or the difference between the program's current $1.5 billion cap and the bill's revised $1.75 billion cap. As of June 13, 2012, the EDA has awarded $977.1 million in urban transit hub tax credits to 18 projects.

The OLS projects that the bill will not trigger a State revenue loss before FY 2015 and after FY 2028. Since capital investments must be incurred after the bill's date of enactment and since the receipt of tax credits is contingent upon project completion, the OLS surmises that no credit reflecting the bill's expanded tax credit eligibility will be claimed until at least FY 2015. Businesses and developers also have ten years in which to apply a tenth of the credit's total value per year. If an urban transit hub credit was approved soon after July 28, 2017 (the last day on which applicants can submit their final tax credit application documents), the last credit could be claimed in the tax year including the second half of 2026, which could be as late as in FY 2028.

Irrespective of the exact magnitude of the bill's revenue loss to the State, taxpayers availing themselves of the tax credit will share their benefit with the federal government. This will be so because taxpayers can deduct their State and local income tax payments on their federal income tax returns. Consequently, a lower New Jersey corporation business tax liability translates into a lower federal deduction, and thus a higher federal income tax liability. At the federal corporation income tax rate of 35 percent, for example, taxpayers receiving a State tax credit will therefore only hold on to 65 percent of the tax credit amount, while the remaining 35 percent of the benefit will accrue to the United States government.

Indirect Fiscal Impact: The bill may generate an indeterminate indirect revenue gain to the State and local governments that may partially offset the direct State revenue loss from and State opportunity cost of providing the tax credits. The OLS, however, does not have the capacity to quantify the bill's secondary effects, since it cannot estimate the number, type, and scale of capital investments that the tax credit will directly spur and their ensuing indirect effect on State and local government tax receipts.

In general, any indirect revenue gain will result from the economic ramifications of tax credit-induced behavior changes. Once New Jerseyans will have income they would not have had absent the tax credit, at least a portion of that additional income will newly circulate in New Jersey's economy. As these ramifications will flow through the economy, they will affect State and local revenue collections. Indirect fiscal effects encompass secondary tax collections from credit-induced capital investments (such as enhanced gross income tax collections from employees whose positions are retained in New Jersey because of the tax credit and increased property tax collections if the investment appreciates the value of a property) and credit-induced spending by all impacted firms and their employees (such as employees whose positions are retained in New Jersey because of the tax credit spending their income on taxable goods and services).

Nonetheless, the OLS points out that not all of the economic and fiscal feedback effects of capital investments benefitting from the credit may represent a gain to the State and affected municipalities. Only the ripple effects caused by credit-induced purchases should enter the fiscal estimate, while those from investments that would also be made absent the credit must be excluded. The exclusion of investments that will happen with or without the credit takes into account that the tax incentive has no economic impact whenever it benefits taxpayers who would invest in a project anyway. In such a scenario, the State will only incur the direct cost of the subsidy, while the capital investment's secondary effects cannot be attributed to the bill.

Notwithstanding that caveat, it is reasonable to expect that most of the indirect effects of tax credits awarded will count as a benefit to the State. This is so because credits can only be awarded if a project passes the net benefit test. As part of that test, the EDA excludes from the analysis the indirect benefits from jobs that are neither "at risk," classified as a "suburban to urban move" or otherwise deemed new jobs to the State. Therefore, only those tax credits will not produce an indirect revenue gain to the State that represent a relocation of jobs from a suburban area of the State to an urban area or that represent an incorrect assessment regarding the likelihood of a job created or retained within New Jersey absent a credit award. It remains unclear, however, whether or not the indirect revenue gains ascribable to the credits will exceed the direct State revenue loss and opportunity cost they will cause.

Lastly, the OLS notes that any estimate of the credit's New Jersey feedback effects must also exclude from the total feedback effects the portion of the credit-induced spending that would leak into other jurisdictions. A New York resident holding a job in New Jersey would have a

New Jersey income tax liability, but most of the New Yorker's private spending might not occur in this State.

Opportunity Costs: Opportunity costs capture the economic and fiscal benefits the economy and the State forego as spending is redirected from one economic activity to another. Given the State's finite resources and its balanced budget requirement, the decision to subsidize certain capital investments in urban transit hubs will invariably divert resources from policy alternatives to which they would have been applied absent the tax credit. Therefore, if, instead of this legislation, the State invested in road construction, for example, the bill would produce a *net* fiscal effect equal to the difference between the total fiscal impact of the amount spent on subsidizing taxpayers' capital investments in urban transit hubs and that of the foregone road construction investment.

Section:	*Revenue, Finance and Appropriations*
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This fiscal estimate has been prepared pursuant to P.L.1980, c.67 (C.52:13B-6 et seq.).