

Testimony of State Treasurer Bradley Abelow
Senate Budget and Appropriations Committee
March 28, 2007

Mr. Chairman. Distinguished members of the Senate Budget and Appropriations Committee.

Good morning.

I am pleased to be back before you again.

With me today are David Rousseau, Budget and Fiscal Policy Advisor to the Governor, Michellene Davis, my Chief of Staff, Charlene Holzbour, the Director of the Office of Management and Budget and Robert Peden, the Deputy Director of OMB.

The Governor's proposed budget of \$33.3 billion is balanced with no new taxes or tax increases. It doesn't rely on devices that mortgage the future to pay today's bills.

Under this budget proposal, \$16.6 billion, about 50 cents of every dollar, is dedicated to relieving the property tax burden in New Jersey. While spending is up seven percent, 80 percent of this increase is directly attributed to a \$1.8 billion increase in property tax relief. The overall growth rate in this budget excluding the increase in property tax relief is less than 2 percent.

Of the \$16.6 billion, \$3 billion is in the form of direct relief to property taxpayers. The largest component of the \$3 billion is \$2 billion for the Homestead Property Tax credits. This relief means an average property tax credit or rebate of \$1,000 for more than 1.9 million New Jersey homeowners. The budget also allocates \$250 million for a larger rebate for tenants, from the current \$75 to up to \$350 for 550,000 tenants with incomes at or below the \$50,000 level.

Property taxpayers will also see relief in the form of increased educational aid to local school districts. Our proposal devotes \$11 billion to support education – a \$580 million increase over the current fiscal year. Approximately \$8 billion of this assistance is in the form of direct aid to school districts, while the balance of \$3 billion represents State assumption of locally-based costs for teacher benefits and debt service on schools. Every district in the State will be eligible for at least a 3 percent increase in aid.

This budget also provides a long overdue increase in municipal aid, including a 2 percent hike in formula aid for all communities and a \$20 million fund to support and incent the consolidation of government services.

This funding infusion is largely attributable to the hard work that the Legislature's special joint reform committees and this Administration devoted to addressing the property tax crisis over the course of this fiscal year.

Another \$730 million in growth is due to higher costs for mandatory expenses associated with contractual obligations in the budget and growth in entitlement programs, such as Medicaid.

With property tax relief and mandatory funding pressures met, the Governor was still able to devote some additional resources to priorities that are vital for our citizens and important to maintaining and enhancing the quality of life in New Jersey.

Tax relief for New Jersey's lowest income families, proposed but ultimately deferred in last year's budget, is contained in the FY 2008 plan. We ask that the Legislature recognize the imperative need to expand the Earned Income Tax Credit Program for the 300,000 workers and their families who stand to gain from it. This change will put \$64 million back in the pockets of working families.

This budget also contains some modest increased investments in areas that touch the lives of our citizens in many different ways.

Total support for New Jersey colleges and universities is funded at \$2.2 billion, including a \$50 million increase in operational aid, and \$22 million more for tuition assistance;

\$30 million to support individuals with developmental disabilities and mental illness;

\$25 million to increase the compensation of community providers;

\$5 million in new funds to help combat the growing problem of autism in New Jersey;

More money for stem cell research, health care access for children, pre-school expansion, arts and history and veterans services.

The modesty of the increases outside of property tax relief should be measured in the context of a \$33 billion budget.

The increase for autism related programs is little more than 1 hundredth of one percent of all spending.

The increased funding for mental health and the developmentally disabled is a little less than one tenth of one percent of the budget.

In order to fund these increases, we've relied upon continued growth in our base revenues next year;

Surplus funds that have accumulated in large part because of sound fiscal management practices and revenue growth that was slightly above anticipated levels;

The availability of \$670 million of sales tax revenues from FY 2007 that was dedicated for property tax relief but reserved for use in FY 2008;

And restraints in government spending.

We have been vigilant in our oversight. We have been resourceful in finding savings.

Since January of 2006, after accounting for necessary staff increases for Homeland Security and DYFS, the State workforce has been reduced by a net of almost 1,300 employees, including the elimination of nearly 400 unclassified positions.

We also have worked hard to reduce the State motor vehicle fleet. Since the beginning of this administration, we have overseen a net reduction of 702 State vehicles, and we will be increasing that total through the end of the current fiscal year.

The newly created Office of Energy Savings has set an aggressive pace for achieving cost savings while keeping an eye toward energy conservation. The Office has set a 5-year goal of reducing energy consumption by ten percent for State facilities, which will save money while minimizing the impact on the environment.

We've netted recurring cost savings by reviewing and renegotiating our natural gas vendor agreements.

We've performed energy reviews and completed adjustments for nine State buildings in Trenton to reduce energy consumption for lighting, heating, cooling, and motors.

Our Division of Property Management and Construction has focused intensely on redeploying government furniture for savings. Contrary to popular belief, this initiative has nothing to do with looking under the seat cushions for spare change.

Rather, DPMC has consolidated the collection of used furniture from various state agencies, centralizing and then redistributing it to those that need furniture. This has enabled the division to avoid the costs of new purchases.

The furniture warehouse consolidation is an outgrowth of a larger warehouse consolidation initiative, which has yielded a recurring lease cost avoidance.

Building on the success of the furniture initiative, DPMC added the recycling of surplus personal computers to its program. In a partnership with the Office of Information Technology (OIT), used computers are refurbished and redeployed, pre-empting the need to purchase new machines.

While savings for furniture, computers, cars, warehouses and energy usage are generally below the public radar, other cost efficiencies are more apparent to the average New Jerseyan.

For example, the Division of Revenue has been able to achieve significant cost savings through the expanded use of electronic business and tax filing /payment systems.

New Jersey taxpayers save about 50 cents every time an electronic return is submitted rather than a paper return. As we are in the midst of tax season, I trust that each of you will file your returns electronically as well.

Mr. Chairman, I introduce all of these economies into my testimony for a couple of reasons. First, I am proud of what we have been able to achieve.

Equally important, though, is that while impressive, the savings alone fall literally billions of dollars short of what's needed to bring structural stability to the budget and fund critical human needs at more appropriate levels. They are the smallest piece of the budgetary pie.

While it is arguably a struggle to find and implement savings strategies, the tougher struggle is aligning priorities with resources.

Let's discuss how the \$33.3 billion budget is allocated and how much of the budget is really "in play" from year to year.

First, we all know that nearly half of the budget, approximately \$16.6 billion, supports property tax relief through direct relief to homeowners and aid to schools and municipalities.

Now, let's look at some of the other larger areas of the budget.

Debt service and dedications for the Transportation Trust Fund, the Garden State Preservation Trust, the Corporation Business Tax and shore protection total \$3 billion.

Health care costs and employer taxes as well as pension and retiree medical costs for State and higher education employees total more than \$2.5 billion.

Our Medicaid program and prescription drug programs total more than \$4 billion.

Our community programs for the citizens with developmental disabilities and mental illness total nearly \$850 million.

Our operating support for higher education and our tuition assistance programs total approximately \$1.5 billion.

These five areas plus property tax relief total nearly \$28.5 billion of the \$33 billion budget.

Looking at our budget from another perspective, we devote all but approximately \$6 billion of the \$33 billion budget on grants and aid and fixed obligations, like debt service and retiree benefits.

Within this \$6 billion is more than \$1 billion in the cost of running the Department of Children and Families; the more than \$1.2 billion cost of running corrections and juvenile justice, the \$450 million to run our centers for the developmentally disabled, psychiatric hospitals and veterans homes, and the \$300 million for State Police and Homeland Security – these four areas total \$3 billion.

The Judiciary and the Legislature account for \$700 million.

Taking into account how we spend our money, it is clear that finding additional savings is extremely difficult and could cripple our ability to provide essential services.

Outside of mandatory funding increases and property tax relief, the Governor chose to devote a minimal amount of funds to additional spending for critical policy initiatives. The Governor noted his dismay over the small amount of funding available, but the truth is we could have devoted less.

But with truths, come consequences and we rejected many options because of those consequences.

What if we had to make additional cuts in our operations? For example, if we eliminated 1,000 of the 12,000 employees that are “at a post,” we would save, at the most, \$50 million. This cut would most likely adversely impact the quality of services demanded by the citizens of New Jersey.

For example, what would happen to college tuition in the absence of giving higher education institutions a \$50 million restoration of a larger operational aid cut in FY 2007?

What would happen to the quality of care, and to the network of health care organizations, if we did not fund a two percent cost of living increase for the community providers?

What if we decided not to provide the \$30 million increase in programs to support individuals with developmental disabilities and mental illness? How do we tell these citizens and their families that there’s no funding for additional placements during the upcoming year?

Allaying the consequences isn’t easy. Neither is finding other ways and places in the budget to fund these priorities.

We have looked at additional areas to reduce the base spending in the budget and we did identify some options to reduce spending.

However, we rejected many options because they would have hurt the quality of life in New Jersey.

We could have made benefit and eligibility changes to the Medicaid program such as not covering services such as prosthetics or other services the federal government does not mandate but that New Jersey has chosen to provide. We looked seriously at these changes but ruled them out because of how they would impact some of New Jersey's most vulnerable citizens.

We could have frozen the income levels for PAAD and forced more people into the Senior Gold Program.

We could have capped the NJSTARS program and made it more difficult for accomplished, but deserving students, to attend college.

We could have deferred the new State Police recruit class and the purchase of new vehicles for road patrols.

Each of my fellow cabinet members will share more specific ideas that were considered within their departments when they appear before this committee.

How we prioritize and pay the State's bills – within the framework of balancing recurring revenues with recurring expenses -- remains the biggest budgetary challenge for both the administration and the Legislature.

We've discussed the expense side of the ledger. Now I would like to address the revenue side for additional perspective.

Let me begin by addressing OLS revenues estimates, which are roughly one percent below those in our proposed budget.

We deeply respect the professionalism and integrity of both fiscal forecasting offices. Since the differences appear to be primarily in the income tax, the April returns should allow us both the opportunity to better clarify the picture once the spring collections are received and taken into account.

That said, we accept that the OLS estimates suggest that we should take a cautionary approach as we work towards adoption of an FY 2008 budget and that we must be mindful that any additional spending or dedication of revenues should be accompanied by an offsetting reduction in spending or increase in real, recurring revenues. When we come back in May, we will accept the responsibility to make changes to ensure that we remain in balance.

For the FY 2008 budget, we forecast \$12.4 billion in revenue from our largest revenue source – the Gross Income Tax. This amount represents 8.3 percent growth over the year

end target of \$11.4 billion. This rate of growth is slower than that of the current year's GIT increase of nine percent, but still represents healthy growth.

The Sales Tax is projected to yield \$8.8 billion for FY 08, a modest growth of 4.2 percent over FY 2007.

We expect that revenue from the Corporation Business Tax., which has greatly bolstered New Jersey's fiscal picture in recent years, will dip considerably in FY 2008 due to tax policy changes, offset in part by underlying growth.

With the expiration of the AMA, the full phasing in of net operating losses and the elimination of the special tax rate on S-corporations, the Corzine administration is sending a clear message to the business community: invest and grow in New Jersey. These taxes hit particular hard at young, growing companies that are investing in and creating jobs in New Jersey.

While some of this revenue is being lost, New Jersey stands to reclaim other substantial revenues as a result of the recent restructuring of the Tobacco Settlement Financing Corporation debt.

As you may recall, New Jersey previously pledged 100 percent of its MSA receipts to bondholders who, in 2002 and 2003 purchased tobacco settlement bonds. Due to the maturation in the market for these bonds, the Tobacco Financing Corporation was successful in lowering the amount of MSA proceeds pledged to bondholders to about 74 percent. This means that the non-pledged portion of the bond will be paid to the State on an annual, ongoing basis.

The benefit to the state in FY 2008 is \$109 million, and the average annual revenue is more than \$55 million.

Notwithstanding this reclaimed revenue stream, income tax growth, sales tax growth and still healthy CBT income, New Jersey's structural fiscal problem is far from solved. Despite constrained spending, our hands remain tied by mandatory expenses that consume a larger and larger share of recurring income.

Our expenses will continue to grow faster than our recurring revenues until we find ways to improve our fiscal position. The Governor has articulated several options for the administration and the Legislature to examine and has focused on reducing the onerous debt service burden.

New Jersey is perilously close to slipping into a state of fiscal paralysis. Our debt service appropriation -- \$2.7 billion -- drains the State Treasury of funds that could otherwise go to meeting critical human needs.

At nearly 10 percent of the total budget, the debt service payment is not unlike the sometimes oppressive minimum payment due on an individual's credit card. Just as a too-

high debt payment inhibits a consumer from buying a car, paying a tuition bill and other household priorities, the State as well is inhibited from investing capital for building new schools, improving our transportation system, acquiring open space and other long term needs of the State.

This budget addresses many needs for FY 2008. What it doesn't do is allow us to invest appropriately in our future. We simply must find a way to loosen the stranglehold that debt service and other recurring expenses place on State finances so that we can invest in our state's future.

I would be happy to answer your questions at this time.