

LEGISLATIVE FISCAL ESTIMATE
SENATE, No. 2263
STATE OF NEW JERSEY
216th LEGISLATURE

DATED: JULY 3, 2014

SUMMARY

- Synopsis:** Raises the gross income tax rate on income exceeding \$1,000,000 to 10.75 percent for a temporary three-year period and restores the State earned income tax credit to 25 percent of the federal credit.
- Type of Impact:** Increase of income revenue deposited in the Property Tax Relief Fund for three fiscal years, followed by an annual loss of revenue deposited into the Fund.
- Agencies Affected:** Department of the Treasury.

Office of Legislative Services Estimate

Fiscal Impact	<u>FY 2015</u>	<u>FY 2016</u>	<u>FY 2017</u>	<u>FY 2018 and Thereafter</u>
State Revenue	\$581.3 to \$615.3 million net gain	\$518.9 to \$550.9 million net gain	\$506.5 to \$533.5 million net gain	\$58.9 million loss growing at 2.5 percent inflation

- The Office of Legislative Services (OLS) estimates that this bill would increase gross income tax revenue deposited in the Property Tax Relief Fund (PTRF) for FY 2015, FY 2016, and FY 2017, followed by an annual loss of revenue deposited into the PTRF beginning in FY 2018. The revenue increases are due to the higher 10.75 percent marginal tax rate, while the revenue decreases are due to the greater Earned Income Tax Credit.
- The OLS notes that the revenue amounts from the 10.75 percent rate increase will be highly volatile and subject to significant annual change. High-income taxpayers are far more dependent on volatile income sources such as capital gains, bonuses, and certain types of business income than are other taxpayers.

BILL DESCRIPTION

Senate Bill No. 2263 of 2014 raises the gross income tax rate on taxable income exceeding \$1,000,000 to 10.75 percent for a temporary three-year-period and restores the State earned

income tax credit to 25 percent of the federal credit. The bill raises the gross income tax rate for taxable years 2014, 2015, and 2016, while it increases the State earned income tax credit for taxable years 2014 and thereafter.

FISCAL ANALYSIS

EXECUTIVE BRANCH

None received.

OFFICE OF LEGISLATIVE SERVICES

The OLS estimates that this bill would increase gross income tax revenue deposited in the PTRF for FY 2015, FY 2016, and FY 2017, followed by an annual loss of revenue deposited into the PTRF beginning in FY 2018. The revenue increases are due to the higher 10.75 percent marginal tax rate, while the revenue decreases are due to the greater Earned Income Tax Credit. The estimates are described separately below.

Gross Income Tax Rate Increase:

Precise figures are not available. The most recently published New Jersey gross income tax (GIT) statistics are for Tax Year 2011. Extrapolating those figures for high income tax payers by assuming annual growth of between 4 percent and 6 percent yields an estimated range of GIT revenue increases between \$550.0 million and \$580.0 million in Tax Year 2014, the first year under this bill. These annual ranges would grow to an estimated \$572.0-\$603.0 million in TY 2015 and \$595.0-\$627.0 million in TY 2016, the third and final year under the bill.

However, the fiscal year revenue distributions will differ from the tax year amounts. There will be no receipts in FY 2014, which will be complete before implementation can begin. In FY 2015 the OLS estimates an approximately 15 percent bonus due to the retroactive implementation of the bill, in which the tax rates are effective beginning January 1, 2014. FY 2015 will collect 100 percent of the TY 2014 tax liability plus an estimated 15 percent of the TY 2015 liability from the first six months of withholding and two quarterly estimated payments in 2015. The OLS estimates this one-time bonus to equal between \$86.0-90.0 million in FY 2015. Accordingly, **the total increased revenue collection in FY 2015 is estimated between \$636.0-\$670.0 million (100 percent of revenues from TY 2014 plus 15 percent of TY 2015). FY 2016 is estimated to raise between \$575.0-\$607.0 million (85 percent of TY 2015 plus 15 percent of TY 2016). FY 2017, the final year of receipts, is estimated to raise between \$506.0-\$533.0 million (85 percent of TY 2016).**

The OLS notes that the revenue amounts from the 10.75 percent rate increase will be highly volatile and subject to significant annual change. High-income taxpayers are far more dependent on volatile income sources such as capital gains, bonuses, and certain types of business income than are other taxpayers. For example, GIT revenue from taxpayers with more than \$1.0 million income rose by 25 percent in TY 2007, the year before the Great Recession, but fell 25 percent in TY 2008 at the onset of the Great Recession.

Earned Income Tax Credit:

The OLS additionally estimates the cost of increasing the State Earned Income Tax Credit (EITC) from 20 percent of the federal credit amount to 25 percent at **annual revenue losses of \$54.7 million in FY 2015 (TY 2014), \$56.1 million in FY 2016 (TY 2015), \$57.5 million in**

FY 2017 (TY 2016), \$58.9 million in FY 2018 (TY 2017) and growing annually by about 2.5 percent thereafter.

The OLS estimate is based on the latest data available from both the Internal Revenue Service (IRS) and the New Jersey Division of Taxation (“division”). According to IRS and division data, of the 599,195 NJ taxpayers claiming a federal EITC in TY 2011, 528,003 taxpayers also filed for a State credit amount. However, of those taxpayers filing for the State benefit, only 466,235 claims (or 80.4 percent) were approved for payment based on an enforcement screening initiative implemented beginning with TY 2011, reflecting a significantly decreased participation rate over the prior year.

In arriving at its \$54.72 million estimate, the OLS relied on IRS EITC program statistics which indicate New Jersey families claimed approximately \$1.2 billion under the federal program in TY 2012. Using these data, the OLS projected the total amount of federal EITC claims for subsequent tax years by assuming a growth rate of 2.5 percent based on IRS “preview” data of the maximum federal credit amounts anticipated for TY 2013. Applying the proposed increase in the State benefit amount (from 20 percent to 25 percent of the federal credit amount) to the adjusted data yielded an estimate of total State EITC program costs which was then discounted to reflect the most recent participation rate data for NJ taxpayers participating in both the State and federal programs.

Under the EITC, the State benefit amount is increased annually reflecting annual adjustments in the federal income eligibility limits and benefit amounts. Should the participation rate in the State program increase or decrease, the OLS estimate would need to be adjusted accordingly.

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