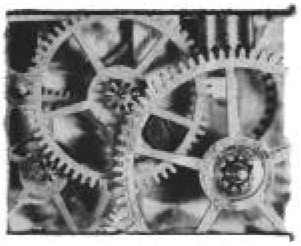

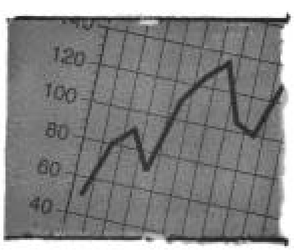

ANALYSIS OF THE NEW JERSEY BUDGET

TAX AND REVENUE OUTLOOK

FISCAL YEAR 2004 - 2005

PREPARED BY OFFICE OF LEGISLATIVE SERVICES
NEW JERSEY LEGISLATURE • MARCH 2004

NEW JERSEY STATE LEGISLATURE

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This report was prepared by the Revenue, Finance and Appropriations Section of the Office of Legislative Services in conjunction with the Legislative Budget and Finance Office. The primary authors were David J. Rosen and Martin Poethke.

Questions and comments may be directed to the OLS Revenue, Finance and Appropriations Section (609-984-6798) or the Legislative Budget and Finance Office (609-292-8030).

THE FY 2004 AND FY 2005 TAX AND REVENUE OUTLOOK

Introduction

This report has been prepared by the Office of Legislative Services (OLS) to assist the Senate Budget and Appropriations Committee and the Assembly Budget Committee as they develop the FY 2005 appropriations act. The OLS revenue estimates reflect a careful review of current State revenue collections, historic revenue collection patterns, and a variety of economic data and forecasts.

The OLS projects that, for FY 2004 and FY 2005, revenues will be $307 million greater than the estimates in the FY 2005 Governor's Budget Recommendation. Specifically:

- For FY 2004, the OLS's revenue estimates are $157 million above the Executive budget estimates (page 4).
- For FY 2005, the OLS's revenue estimates are $150 million above the Executive budget estimates (page 5).

In addition, the OLS observes that while tax revenues have begun to rebound from the severe downturn that struck in FY 2002, the State remains dependent on substantial non-recurring revenues, most prominently the securitization of future State revenue streams, and on the enactment of new taxes and fees.

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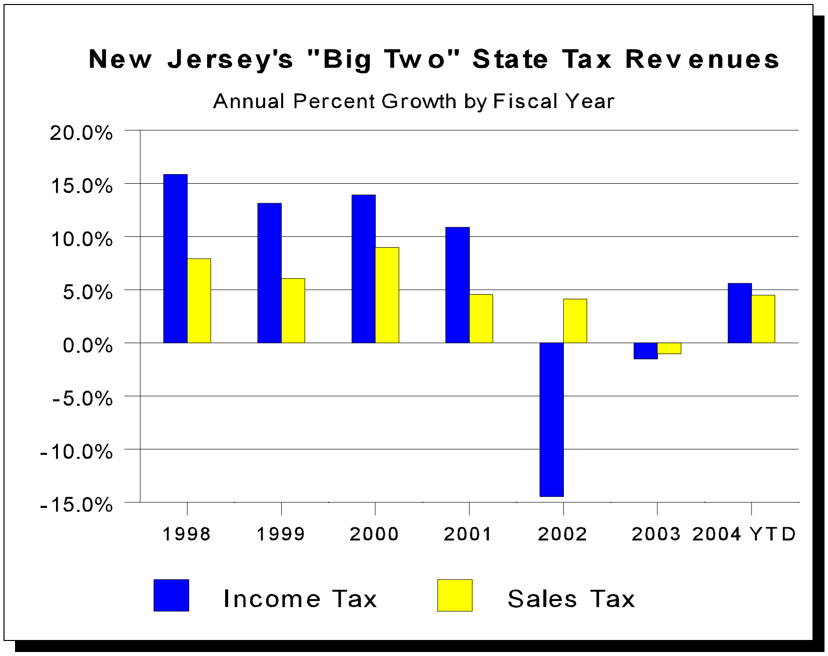
Recap: FY 2004 Collections to Date

Figure 1



The bleeding has stopped. State tax revenue collections, which had suddenly turned anemic in FY 2002, are showing sure signs of recovery in FY 2004. The recent history of the gross income tax and the sales tax, which typically account for between 55% and 65% of total budgeted revenues, is displayed in Figure 1. Specifically:

- Annual Income tax growth averaged over 13.0% from FY 1998 to FY 2001, but plummeted by an unprecedented 14.4% in FY 2002 and fell another 1.5% in FY 2003. Through the end of February, FY 2004 collections are up 5.6% year-to-date.

- The sales tax declined by 1.0% in FY 2003 from an FY 2002 level that had been inflated by the tax amnesty program. However, adjusting for this effect, the underlying growth of about 3.4% was among the lowest in a decade. Through the end of February, FY 2004 collections are up 4.5% year-to-date.

Figure 2 contains a more detailed display of current FY 2004 revenue collections through the end of February. In addition to the encouraging news about the income tax and the sales tax, key points include:

- Corporation business taxes are running 11.6% ahead of last year's levels, but declines are expected in the latter months of the fiscal year due to certain timing effects of the recent law change.

- Revenues from casinos, cigarettes, and real estate sales are up strongly due in part to tax rate increases enacted last year.

- Inheritance tax revenues have rebounded from a sharp decline in FY 2003.

Recap: FY 2004 Collections to Date

Figure 2
FY 2004 Year-To-Date
Selected Revenue Comparison
Through the End of February 2004 vs. February 2003

($ millions)

Revenue Source	FY 2003 Actual Year-To-Date	FY 2004 Actual Year-To-Date	FY 2004 Actual Year-To-Date % Change	FY 2004 Year-End Treasury % Change Target
Gross Income Tax	$4,019.3	$4,245.5	5.6%	7.5%
Sales Tax *	3,480.7	3,638.0	4.5%	5.0%
Corporation Business Tax	943.8	1,053.6	11.6%	(11.0)%
Lottery	480.1	503.1	4.8%	3.2%
Motor Fuels *	305.0	323.2	6.0%	1.7%
Motor Vehicle Fees	277.1	73.4	(73.5)%	(20.9)%
*MV Fees (Total) ** *	*277.1*	*275.3*	*(0.7)%*	*(2.4)%*
Casino	227.3	292.0	28.4%	32.5%
Inheritance Taxes	290.4	363.7	25.2%	14.5%
Insurance Premiums	144.2	116.5	(19.2)%	15.2%
Cigarette (Budgeted)	254.1	351.4	38.3%	24.3%
*Cigarette (Total)****	*404.1*	*501.4*	24.1%	*18.4%*
Petroleum Products *	127.2	121.7	(4.3)%	(4.4)%
Alcohol Excise *	44.6	46.5	4.3%	3.5%
CBT -- Banks & Financials	53.8	57.4	6.7%	9.0%
Realty Transfer *	68.5	124.0	81.0%	71.1%

Sources: Year-To-Date revenues are from Treasury's monthly cash reports. The year-end Treasury percentage change target is based on the February revised revenue estimates for FY 2004 contained in the proposed FY 2005 budget.

** Revenues represent seven months of cash collections. All others represent eight months of cash collections.*

*** Motor Vehicle Fees (Total) in FY 2004 includes the dedication of $201.9 million off-budget for the NJ Motor Vehicle Commission (P.L.2003, c.13).*

**** Cigarette (Total) includes $150 million deposited directly into the off-budget Health Care Subsidy Fund in both FY 2003 and FY 2004.*

Fiscal Year 2004 Revenue Estimates

Figure 3
Fiscal Year 2004 Revenue Estimates
($ millions)

	Approp. Act (7/1/03)	Executive Revised		OLS	
		Amount (Feb.)	$ Change From Approp.	Amount (March)	OLS vs. Exec.
Gross Income Tax	$7,130	$7,240	$110	$7,300	$60
Sales Tax	6,165	6,235	70	6,255	20
Corporation Business Tax	2,055	2,247	192	2,300	53
Cigarette Tax	635	595	(40)	625	30
Tobacco Settlement Fund	1,612	1,612	0	1,612	0
Other Revenues*	6,408	6,459	52	6,453	(6)
Grand Total, All Funds	$24,005	$24,389	$384	$24,546	$157

See Appendix for additional detail. Numbers may not add due to rounding.
** See specific differences for Other Revenues in Figure 11 on page 12.*

Figure 3 presents the FY 2004 revenue certification from the Appropriations Act (July 2003), the Executive's February revisions as presented in the Governor's Budget Recommendation, and the OLS's forecast. Highlights of the revenue estimates include:

FY 2004 Executive:

- In February, the Executive revised estimates for all revenues upward by a net $384 million from the level certified in the FY 2004 Appropriations Act.
- The estimate for the income tax is up $110 million.
- The estimate for the sales tax is up $70 million.
- The estimate for the corporation business tax is up $192 million.
- The estimate for the cigarette tax is down $40 million.

FY 2004 Office of Legislative Services:

- The OLS's total revenue estimates for FY 2004 are **$157 million above** the Executive's.
- The OLS's estimate for the income tax is $60 million higher than the Executive's.
- The OLS's estimate for the sales tax is $20 million higher than the Executive's.
- The OLS's estimate for the corporation business tax is $53 million higher than the Executive's.
- The OLS's estimate for the cigarette tax is $30 million higher than the Executive's.

Fiscal Year 2005 Revenue Estimates

Figure 4
Fiscal Year 2005 Revenue Estimates
($ millions)

	Executive		OLS		Difference OLS vs. Exec.
	Amount	Change	Amount	Change	
Gross Income Tax	$7,843	8.3%	$7,920	8.5%	$77
Sales Tax	6,575	5.5%	6,600	5.5%	25
Corporation Business Tax	2,403	7.0%	2,461	7.0%	58
Cigarette Tax	708	19.0%	730	16.8%	22
New Revenue Securitizations	1,520	--	1,520	--	0
Other Revenues*	7,208	11.6%	7,176	11.2%	(32)
Grand Total, All Funds	$26,258	7.7%	$26,407	7.5%	$150

See Appendix for additional detail. Numbers may not add due to rounding. OLS change is from OLS FY 2004.
** See specific differences for Other Revenues in Figure 12 on page 13.*

Figure 4 presents the Executive's FY 2005 revenue estimates as presented in the Governor's Budget Recommendation and the OLS's forecast. Highlights of the revenue estimates include:

FY 2005 Executive:

- The Executive expects total revenues to grow by $1.87 billion, or 7.7% over FY 2004.
- The estimate for the income tax is up $603 million over FY 2004, or 8.3%.
- The estimate for the sales tax is up $340 million over FY 2004, or 5.5%.
- The estimate for the corporation business tax is up $156 million over FY 2004, or 7.0%.
- The estimate for the cigarette tax is up $113 million over FY 2004, or 19%, including an assumed tax rate increase.
- The Executive's revenues include $1.52 billion in "new revenue securitizations".

FY 2005 Office of Legislative Services:

- The OLS's total revenue estimates for FY 2005 are **$150 million above** the Executive's.
- The OLS's estimate for the income tax is $77 million higher than the Executive's.
- The OLS's estimate for the sales tax is $25 million higher than the Executive's.
- The OLS's estimate for the corporation business tax is $58 million higher than the Executive's.
- The OLS's estimate for the cigarette tax is $22 million higher than the Executive's.
- The OLS assumes the realization of the securitization for comparability purposes. The securitization would require legislation.

Budgetary Impact of the OLS Revenue Estimates

The OLS estimates FY 2004 revenues will be $157 million above the Executive estimates and FY 2005 revenues will be $150 million above the Executive estimates. Combined over the two year period, the OLS estimates $307 million more than the Executive.

As part of its annual analysis, the OLS typically recalculates the State's year-end budgeted balance based solely on the revenue forecast differences between the Executive and the OLS. Figure 5 assumes that the spending plan and tax law changes in the FY 2005 Executive budget will be followed. However, any calculation of the actual balance must take into account numerous spending decisions as well as anticipated revenue. Decisions on these and other matters will be made by the Executive, both budget committees and the full Legislature during the next three months.

Figure 5
OLS Adjusted FY 2005
Year-End Balance

Executive Estimate	$400,000,000
OLS Revenue Adjustment	$307,000,000
OLS Estimate	$707,000,000

As is shown in Figure 5, the Executive estimates an FY 2005 year-end balance of $400 million. All other things being equal, the higher OLS revenue estimates would produce a year-end balance of **$707 million**, $307 million more than the Executive's estimates.

It is premature to draw conclusions about actual year-end balances from this analysis of State revenues. Projections of the State's year-end balance are a static image of a moving target. Because of the large number of changes that occur in both spending and revenues throughout any fiscal year, the surplus changes significantly between the enactment of the annual appropriations act, the end of the fiscal year and the final review by State auditors.

Gross Income Tax

Figure 6

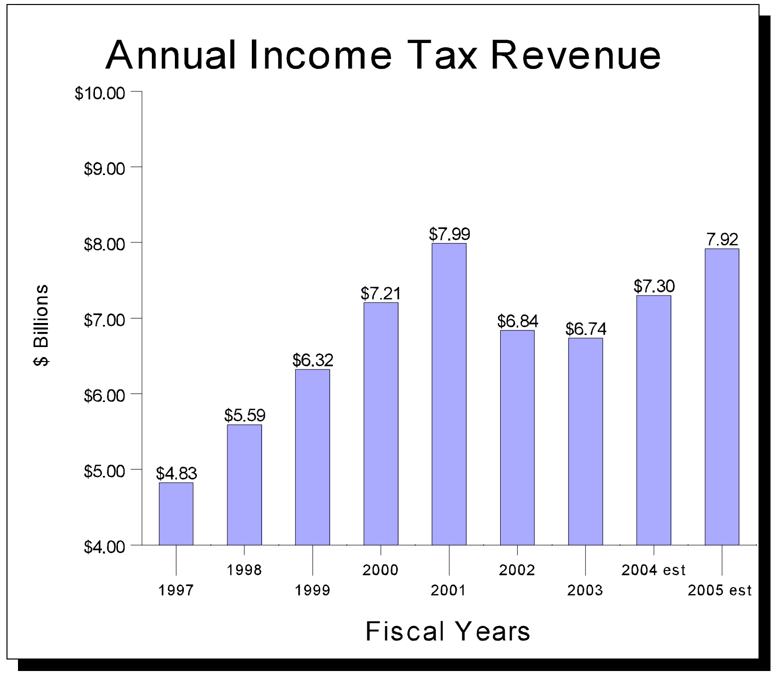
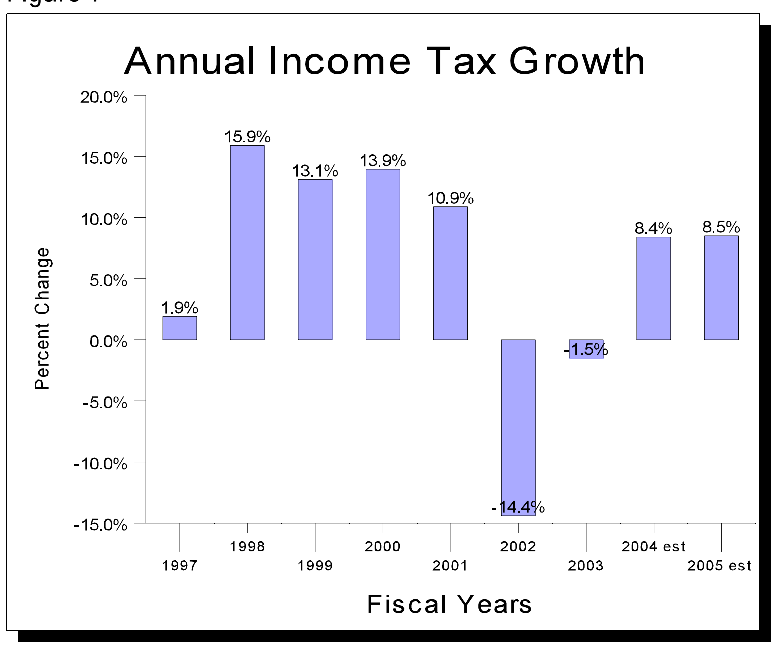


Figure 7



The gross income tax (GIT) is emerging from an unprecedented period in its history. Prior to FY 2002 there had been only one year in which this revenue had declined (and that was for technical, not economic, reasons). Then, in FY 2002, the GIT tumbled 14% and followed that with a second year of decline in FY 2003 (See Figures 6 and 7).

Previous editions of the *Tax and Revenue Outlook* posited an explanation for this decline, pointing specifically at non-wage income of higher income taxpayers. The recent release of Tax Year 2001 *New Jersey Statistics of Income* data, confirms the accuracy of those explanations. Capital gains income declined by a remarkable 60% between 2000 and 2001. Partnership income fell by 10%. The average tax payment of the top 1% of resident taxpayers dropped by 22%, accounting for an $800 million State revenue loss. For additional figures, see the discussion, *Income Tax Snapshots: Tax Years 1988 to 2001*, in the appendix.

In FY 2004, we are seeing a rebound from the revenue declines of the last two years. Total collections through the end of February are up 5.6%. Collections from employer withholding of employee wages are up over 8.0%. Importantly, collections from non-wage income sources may also have turned the corner. Quarterly estimated payments, which were down for two straight years, grew by about 5.0% in the most recent December/January payment period.

In light of the improving monthly collections data for wage and non-wage income, and considering the Council of Economic Advisors' estimate (See the Council's report in the appendix) that growth in personal income and employment will accelerate, both the Executive and the OLS are estimating solid growth in the GIT this year and next year.

Gross Income Tax (Continued)

GIT Components

In analyzing the GIT, we look at four basic components of the revenue stream:

Withholding Collections: Withholding is paid throughout the year by employees when their employers deduct a portion from each paycheck, bonus and the like. This is the largest component of income tax collections. Withholding receipts are up 8.4% so far in FY 2004. The OLS believes this growth will continue in FY 2004 and FY 2005.

Estimated Payments: These payments generally are made in the months of April, June, September, and December/January by taxpayers with significant non-wage income. Estimated tax payments fell 25% in FY 2002 and fell another 7% in FY 2003. That unprecedented decline appears to be over, as the most recent payment in the December/January period grew by 5.0%. The OLS believes this growth will continue in FY 2004 and will accelerate further in FY 2005.

Despite growth, neither the FY 2004 nor the FY 2005 gross income tax is expected to reach the revenue attained in FY 2001.

Final Payments: The linchpin for any GIT estimate is the important final tax payments that come in during April and May. As with estimated payments, taxpayers who must make large final tax payments generally have significant sources of non-wage income. In line with the estimated payments, total final tax payments fell by 23% in FY 2002 and fell by nearly 10% in FY 2003. This has been the dreaded "April Surprise" that caused late-year fiscal stress in balancing the State budget the last two years (During FY's 1998 to 2001, the April Surprises were substantial windfalls of additional cash). The OLS believes final payments will show an increase in FY 2004, as suggested by the solid increase in the most recent quarterly estimated payments. The OLS believes this growth will accelerate in FY 2005.

Refund Payments: Refund payments are paid by the State, largely in the spring and summer, to taxpayers whose April 15 tax filings show payments exceeding their tax liability. Refund payments jumped by 17% in FY 2003. Now that taxable incomes appear to be growing again, the OLS believes refund payments will be relatively stable in FY 2004 and will grow moderately in FY 2005.

FY 2004

The Executive estimates $7.24 billion, or 7.5% growth over FY 2003. The OLS estimates somewhat higher revenues of $7.3 billion, an 8.4% growth rate. The OLS estimate is $60 million above the Executive's.

This $60 million difference between the OLS and the Executive is small and does not reflect a different view of the economy. The OLS estimate is based primarily on current trends for the major components of the GIT.

FY 2005

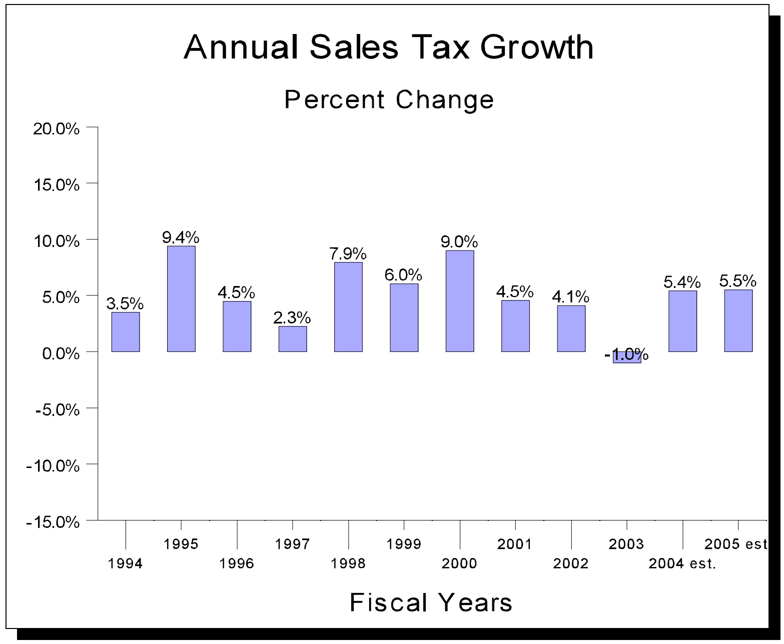
The Executive is estimating $7.843 billion in GIT revenue for FY 2005, an increase of 8.3% over FY 2004. The OLS is estimating $7.92 billion, or 8.5% growth over a higher FY 2004 base amount. The OLS's total is $77 million greater than the Executive's total.

As with the modest GIT revenue difference between the Executive and the OLS in FY 2004, the $77 million difference in FY 2005 does not indicate a fundamental difference in economic growth assumptions. The difference is due largely to a slightly higher FY 2004 base in the OLS estimates.

Sales Tax

The Sales tax provides a measure of stability to annual revenue collections. Growth rates generally fall within a narrow range, in contrast to the greater volatility of the gross income tax. Due to the mild recession that began in the Spring of 2001, sales tax revenue growth slipped in FY 2003, as is shown in Figure 8. However, after adjusting for $81 million in net tax amnesty receipts received in the Spring of 2002, underlying sales tax collections actually grew by 2.7% in FY 2002 and by 3.4% in FY 2003. Current trends suggest a return to the historical average of about 5.0% growth.

Figure 8



FY 2004: Sales tax collections through the end of February are running 4.5% ahead of the same period one year ago. The Executive expects the growth to accelerate somewhat in the spring, bringing total growth by the end of FY 2004 to about 5.0% and total collections to $6.235 billion. The OLS agrees that revenue growth should increase in the spring, especially since last spring's collections were weak due to public concerns over the start of the Iraq war. Relative to last spring's weak baseline, the OLS is somewhat more optimistic than the Executive and expects year-end growth to reach 5.4%. That slightly higher rate will yield an additional $20 million above the Executive's estimate, or an FY 2004 total of$6.255 billion.

FY 2005: The Executive and the OLS both anticipate improving sales tax growth in FY 2004 to continue through FY 2005. The Executive anticipates collections of $6.575 billion, or 5.5% growth. In light of the Council of Economic Advisors' forecast of improving retail sales and new vehicle registrations (See the appendix, beginning on page A11), the OLS concurs with the forecast of 5.5% sales tax revenue growth in FY 2005. The OLS's estimate of $6.0 billion is $25 million above the Executive's estimate due to a slightly higher FY 2004 base.

Corporation Business Tax

The FY 2004 revenue certification anticipated that corporation business tax (CBT) revenues would decline, because a number of the features of the Business Tax Reform Act of 2002 were designed to pump money into FY 2003. It still appears that the CBT will decline in FY 2004, but by less than previously anticipated. A further decline would be anticipated for FY 2005, but the Governor's proposal to continue the disallowance of the use of Net Operating Losses (NOLs) and to decouple from the enhanced federal expensing law will eliminate that decline. The OLS forecasts for the CBT are higher than the Executive's by $53 million in FY 2004 and by $58 million in FY 2005. Forecasting the CBT, which has always been difficult, is now more problematic because of the complexity of the new law and the minimal data about its impact.

Cigarette Tax

The cigarette tax rate has been increased a number of times in recent years and the Executive is proposing an additional increase for FY 2005. The $0.80 per pack tax in effect through FY 2002 was increased by $0.70 per pack in FY 2003 and by $0.55 per pack in FY 2004. The Executive is proposing legislation for a $0.45 per pack increase for FY 2005. With this increase, the tax on a pack of cigarettes will be $2.50.

FY 2004

The FY 2004 Appropriations Act assumed total on-budget and off-budget revenues of $785 million, an increase of 25% over the prior year due to the $0.55 per pack tax increase. With the release of the Governor's Budget Message, the Executive has reduced the FY 2004 revenue estimate to $745 million. This represents a $40 million reduction that implies growth of only about 18% from the FY 2003 level (See Figure 9 below).

The OLS does not believe the Executive's downward revision is warranted. As Figure 2 (page 3) shows, total cigarette tax revenues in FY 2004 are up by more than 24% through the end of February, in line with the original certified target in the appropriations act. For the Executive's downward revision to hold, underlying sales and revenues must decline by 8% in FY 2004 (See Figure 9). While underlying sales declines in the range of 2% to 4% have occurred in recent years, there is no sign of an 8% decline. Indeed, the Executive's estimate for FY 2005 implicitly assumes an underlying decline of only about 3% in spite of an additional tax rate increase.

Accordingly, the OLS estimates $775 million in total on- and off-budget cigarette tax revenues for FY 2004, $30 million above the Executive's estimate. This amount assumes an underlying 3% sales decline offset by the effect of the $0.55 per pack tax increase. Total revenues are estimated to increase by 23% over FY 2003.

Figure 9
Cigarette Tax Revenue Estimates

$ Millions	FY 2003	FY 2004		FY 2005	
	Actual	Exec.	OLS	Exec.	OLS
FY 2003 $1.50/Pack	$629	$580	$610	$563	$590
Percent Change	--	*-8%*	*-3%*	*-3%*	*-3%*
FY 2004 $0.55/Pack Increase	--	$165	$165	$160	$160
Percent Change	--	--	--	*-3%*	*-3%*
FY 2005 $0.45/Pack Increase	--	--	--	$135	$130
Grand Total	$629	$745	$775	$858	$880
Percent Change	--	*18%*	*23%*	*15%*	*14%*
HCSF Dedication	$150	$150	$150	$150	$150
On-Budget Total	$479	$595	$625	$708	$730

FY 2003 revenue estimated by OLS. HCSF = Health Care Subsidy Fund, an "off-budget" account.

Cigarette Tax, Continued

FY 2005

The Executive estimates total cigarette tax revenues will grow to $858 million in FY 2005, or an increase of about 15% from their FY 2004 estimate. This increase includes the impact of the proposed $0.45 per pack tax hike (See Figure 9). The Executive assumes underlying cigarette revenues will decline by about 3%, but that total collections will grow due to an additional $135 million from the tax rate increase.

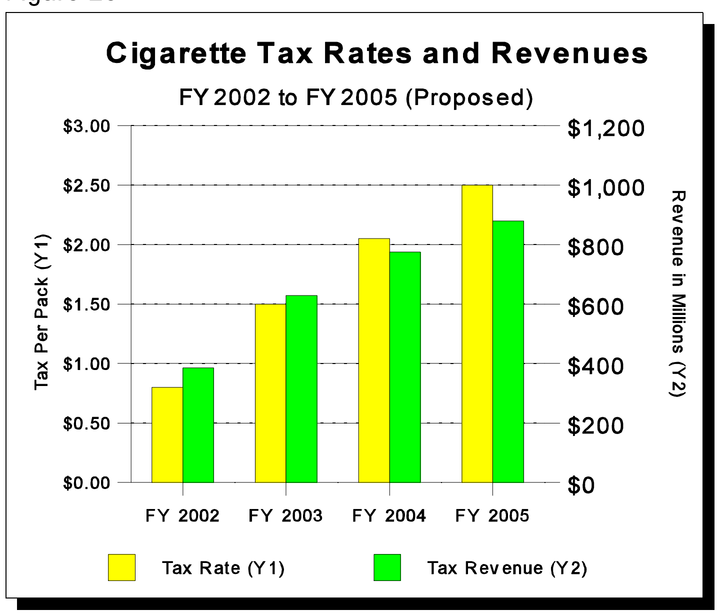
The OLS estimates an FY 2005 total revenue of $880 million, $22 million above the Executive. This difference is not due to a significant divergence in FY 2005 growth assumptions, but rather it is due to OLS's higher FY 2004 estimated base.

The OLS believes the Executive's implicit underlying assumption of a 3% revenue decline (see Figure 9) is reasonable and well within the experience of recent years. The Executive's estimate of $135 million in additional cigarette tax revenue from the $0.45 rate increase is also reasonable. That amount equals approximately $3.0 million of new revenues for each additional penny of tax per pack. By comparison, actual FY 2003 total cigarette tax revenues brought in about $4.2 million per penny of tax and current FY 2004 collections are effectively raising about $3.8 million per penny of tax. The fiscal estimates for the $0.55 per pack increase in FY 2004 reflected about $3.2 million per penny in new revenues. So, the Executive's assumption of a further decline in the "productivity" of an increased tax rate is appropriate.

The OLS is slightly more cautious about the impact of an additional $0.45 per pack onto what is already the nation's highest cigarette tax rate. Accordingly, the OLS is estimating the Executive's proposed $0.45 per pack rate increase will generate $2.9 million per penny in new revenues, or $130 million overall.

Figure 10 displays the decline in the productivity of the increasing tax per pack. The bars representing the increasing tax rate are growing more rapidly than the bars representing the increasing tax revenues.

Figure 10



Health Care Subsidy Fund

The above discussion regarding cigarette tax collections focusses on the total tax rate and the total collections, both on- and off-budget. Implicit within that discussion, and shown in Figure 9, is the statutory requirement that the first $150 million of cigarette tax collections be deposited into the Health Care Subsidy Fund.

Other Revenue Differences

Figures 11 and 12 on the next two pages display the other revenues for which the OLS and the Executive estimates differ. Most of the differences reflect slightly variant interpretations of current revenue growth trends in FY 2004.

Figure 11
FY 2004 Revenues
($ Millions)

Revenue Source	Executive Amount	OLS Amount	Diff.	OLS Comment
Inheritance Taxes	$510.0	$530.0	$20.0	Current trends suggest a higher amount is likely.
Realty Transfer Tax	$187.0	$195.0	$8.0	Current trends suggest a higher amount is likely.
Gubernatorial Elections Fund	$1.5	$1.0	($0.5)	Collections have not exceeded $1 million in over a decade.
Alcohol Beverage Excise Tax	$86.0	$85.0	($1.0)	Current trends suggest a lower amount is likely.
Insurance Premiums	$430.0	$420.0	($10.0)	Current trends suggest a lower amount is likely.
Casino Revenue Fund	$459.9	$448.7	($11.2)	Current trends suggest a lower amount is likely.
Hotel Occupancy Tax	$111.4	$100.0	($11.4)	Current trends suggest a lower amount is likely.
Total Difference, FY 2004			($6.1)	

Other Revenue Differences

Figure 12
FY 2005 Revenues
($ Millions)

Revenue Source	Executive Amount	OLS Amount	Diff.	OLS Comment
Realty Transfer Tax	$275.0	$285.0	$10.0	OLS projects a higher amount due to a higher FY 2004 base.
Gubernatorial Elections Fund	$1.5	$1.0	($0.5)	Collections have not exceeded $1 million in over a decade.
Alcohol Beverage Excise Tax	$88.0	$87.0	($1.0)	OLS projects a lower amount due to a lower FY 2004 base.
Insurance Premiums	$473.0	$470.0	($3.0)	OLS projects a lower amount due to a lower FY 2004 base.
CBT -- Banks and Financial Institutions	$144.0	$140.0	($4.0)	The OLS is more cautious with this revenue's future projection due to historic volatility.
Casino Revenue Fund	$478.9	$467.0	($11.9)	OLS projects a lower amount due to a lower FY 2004 base.
Inheritance Taxes	$572.0	$550.0	($22.0)	The OLS is more cautious with this revenue's future projection due to historic volatility.
Total Difference, FY 2005			($32.4)	

Revenue Changes Requiring Legislation

Figure 13 displays the Executive's new revenue proposals that will require Legislative enactment. The Governor's Budget Recommendation assumes, and the OLS accepts for the purposes of this report, the enactment and successful implementation of these proposals. This list does not include other non-revenue-generating Legislative enactments that will be needed to support the Governor's Budget Recommendation.

Figure 13
FY 2005 Revenues Requiring Legislation
($ Millions)

Revenue Source	Executive Amount	Source of Money	Comment/History
Corporation Business Tax - Continue the disallowance of the use of net operating loss (NOL) carry forwards for two additional years	$275.0	Corporations that will not be able to reduce their current tax liability by applying prior NOLs	The Business Tax Reform Act of 2002 disallowed the use of NOLs for two years. **Legislation required.** *
Petro-Chemical Environmental Impact Fee	$150.0	Details not provided	**Legislation required.**
Cigarette Tax Increase from $2.05 to $2.50 a pack	$135.0	Purchasers of cigarettes	Tax was last raised in July 2003.** **Legislation required.**
Motor Vehicle Fee Acceleration	$90.0	Owners of newly registered vehicles	**Legislation required.**
Increase in Realty Transfer rates for properties sold at $150,000 or more	$70.0	Sellers of real property	Tax was last raised in July 2003. **Legislation required.**
Maintain Transitional Energy Facilities Assessment (TEFA) which is phasing out	$54.0	Utility ratepayers	TEFA was part of 1997 energy tax reforms; Intended to phase out in five years, it was extended in 2001. **Legislation required.**
Increased Annual Hospital Assessment from 0.53% to 0.70%	$50.0	All hospitals	**Legislation required.**
New Motor Vehicle Surcharge	$50.0	Drivers guilty of unsafe driving	**Legislation required.** **
Hospital Outpatient Visit $5.00 Fee	$34.0	Details not provided	**Legislation required.**

Revenue Changes Requiring Legislation

Figure 13
FY 2005 Revenues Requiring Legislation
($ Millions)

Revenue Source	Executive Amount	Source of Money	Comment/History
Wireless Communications Assessment	$33.0	Details not provided	Legislation required.
Ambulatory Medical Facilities Assessment	$31.0	Details not provided	Legislation required.
New 1% Assessment on Homes Purchased for at least $1,000,000	$24.0	Purchasers of homes	Legislation required.
Increase Spill Fund Tax Rate from 1.5 to 3.1 cents per barrel; remove cap	$20.0	Assessed on the first transfer of hazardous substances and petroleum products	Current rate set in 1987 with liability capped at 125% of 1986 tax on petroleum products and 100% of 1986 tax on hazardous substances. Legislation required.
New Tire Clean-up Surcharge set at $1.50 per tire	$12.0	Purchasers of tires	Despite the name, less than 20% of anticipated revenue will be used for tire clean-up in FY 2005. Legislation required.
New Hazardous Waste Disposal $25 per ton tax	$11.0	Operators of hazardous waste treatment and disposal facilities	Legislation required.
Extend Outdoor Advertising Tax	$10.0	Billboard Owners	Tax adopted in July as one-year measure. Legislation required.
New tax surcharge of $10 per pound of Air Toxics emissions	$6.0	Major stationary sources that emit air toxics	Legislation required.
Total, FY 2005	$1,055.0		

* The corporation business tax changes proposed by the Executive also include the assumption of a State decoupling from the enhanced federal expensing law (IRS code section 179). However, no dollar amount attributable to this proposed tax law change has been provided at this time.

** Beginning in FY 2007, the new cigarette tax revenues and the new motor vehicle surcharge revenues will be used for debt service on the proposed $1.52 billion in revenue securitization that is supporting the FY 2005 budget. The securitization proposal, while not a permanent change in tax law, will also require Legislative action.

Appendix Contents:

Detailed Fiscal Year 2004 Revenue Estimates
$ Millions

Revenue Source	Approp. Act	Executive Revised	OLS	Diff: OLS - Executive
Major Taxes:				
Sales Tax, Total	$6,165.0	$6,235.0	$6,255.0	$20.0
Corporation Business Tax, Total	2,055.0	2,247.0	2,300.0	53.0
Corporation Business Tax, Base	*2,055.0*	*2,247.0*	*2,300.0*	*53.0*
Corporation Business Tax, Energy Contribution	*0.0*	*0.0*	*0.0*	*0.0*
Motor Fuels	544.0	540.0	540.0	0.0
Motor Vehicle Fees	233.1	233.1	233.1	0.0
Inheritance Taxes	433.0	510.0	530.0	20.0
Insurance Premiums	420.0	430.0	420.0	(10.0)
Cigarette	635.0	595.0	625.0	30.0
Petroleum Products Gross Receipts	225.0	205.0	205.0	0.0
Corporation Business - Banks and Financial	131.0	140.0	140.0	0.0
Alcoholic Beverage Excise	83.0	86.0	85.0	(1.0)
Realty Transfer	172.0	187.0	195.0	8.0
Savings Institutions	5.0	0.0	0.0	0.0
Tobacco Products Wholesale	13.0	10.0	10.0	0.0
Public Utilities Excise	8.7	8.7	8.7	0.0
Subtotal, Major Taxes	$11,122.8	$11,426.8	$11,546.8	$120.0
Misc. Taxes, Fees and Revenues				
Public Utility Taxes (State retention)	$69.0	$69.0	$69.0	$0.0
Transitional Energy Facility Assessments	218.3	211.0	211.0	0.0
Medicaid Uncomp. Care Reimbursement	455.1	505.1	505.1	0.0
Hotel Occupancy Tax	111.4	111.4	100.0	(11.4)
Other	1,496.7	1,444.3	1,444.3	0.0
Subtotal, Misc. Revenues	$2,350.5	$2,340.8	$2,329.4	($11.4)
Interfund Transfers				
State Lottery Fund	$793.0	$790.0	$790.0	$0.0
Tobacco Settlement Fund	1,612.0	1,612.4	1,612.4	0.0
Unclaimed Personal Property Trust Fund	172.4	164.8	164.8	0.0
Other	311.1	293.1	293.1	0.0
Subtotal, Interfund Transfers	$2,888.5	$2,860.3	$2,860.3	$0.0
TOTAL GENERAL FUND	$16,361.8	$16,627.9	$16,736.5	$108.6
Property Tax Relief Fund (Income Tax), Total	$7,130.0	$7,240.0	$7,300.0	60.0
Casino Revenue Fund	448.7	459.9	448.7	(11.2)
Casino Control Fund	62.7	59.4	59.4	0.0
Gubernatorial Elections Fund	1.5	1.5	1.0	(0.5)
GRAND TOTAL, ALL FUNDS	$24,004.7	$24,388.7	$24,545.6	$156.9

Detailed Fiscal Year 2005 Revenue Estimates
$ Millions

Revenue Source	Executive	% Change	OLS	% Change	Diff: OLS - Executive
Major Taxes:					
Sales Tax, Total	$6,575.0	5.5%	$6,600.0	5.5%	$25.0
Corporation Business Tax, Total	2,403.2	7.0%	2,461.2	7.0%	58.0
Corporation Business Tax, Base	*2,117.0*		*2,175.0*		*58.0*
Corporation Business Tax, Extend NOL Susp.	*275.0*		*275.0*		*0.0*
Corporation Business Tax, Energy Contribution	*11.2*		*11.2*		*0.0*
Motor Fuels	549.0	1.7%	549.0	1.7%	0.0
Motor Vehicle Fees	323.1	38.6%	323.1	38.6%	0.0
Inheritance Taxes	572.0	12.2%	550.0	3.8%	(22.0)
Insurance Premiums	473.0	10.0%	470.0	11.9%	(3.0)
Cigarette	708.0	19.0%	730.0	16.8%	22.0
Petroleum Products Gross Receipts	205.0	0.0%	205.0	0.0%	0.0
Corporation Business - Banks and Financial	144.0	2.9%	140.0	0.0%	(4.0)
Alcoholic Beverage Excise	88.0	2.3%	87.0	2.4%	(1.0)
Realty Transfer	275.0	47.1%	285.0	46.2%	10.0
Tobacco Products Wholesale	10.0	0.0%	10.0	0.0%	0.0
Public Utilities Excise	8.7	0.0%	8.7	0.0%	0.0
Subtotal, Major Taxes	$12,334.0	7.9%	$12,419.0	7.6%	$85.0
Misc. Taxes, Fees and Revenues					
Public Utility Taxes (State retention)	$69.0	0.0%	$69.0	0.0%	$0.0
Transitional Energy Facilities Assessment	211.0	0.0%	211.0	0.0%	0.0
Medicaid Uncomp. Care Reimbursement	519.9	2.9%	519.9	2.9%	0.0
Hotel Occupancy Tax	86.8	(22.1)%	86.8	(13.2)%	0.0
New Environmental Fees and Tire Cleanup	179.3	--	179.3	--	0.0
New Revenue Securitizations	1,520.0	--	1,520.0	--	0.0
Other New Treasury Revenues	86.3	--	86.3	--	0.0
Other	1,526.0	5.6%	1,526.0	5.6%	0.0
Subtotal, Misc. Revenues	$4,198.3	79.4%	$4,198.3	80.2%	$0.0
Interfund Transfers					
State Lottery Fund	$795.0	0.6%	$795.0	0.6%	$0.0
Unclaimed Personal Property Trust Fund	194.1	17.8%	194.1	17.8%	0.0
Tobacco Settlement Fund	0.0	(100.0)%	0.0	(100.0)%	
Other	349.1	19.1%	349.1	19.1%	0.0
Subtotal, Interfund Transfers	$1,338.2	(53.2)%	$1,338.2	(53.2)%	$0.0
TOTAL GENERAL FUND	$17,870.5	7.5%	$17,955.5	7.5%	$85.0
Property Tax Relief Fund (Income Tax), Total	$7,843.0	8.3%	$7,920.0	8.5%	77.0
Casino Revenue Fund	478.9	4.1%	467.0	4.1%	(11.9)
Casino Control Fund	63.7	7.3%	63.7	7.3%	0.0
Gubernatorial Elections Fund	1.5	0.0%	1.0	0.0%	(0.5)
GRAND TOTAL, ALL FUNDS	$26,257.6	7.7%	$26,407.2	7.6%	$149.6

Public Utility Tax Revenue

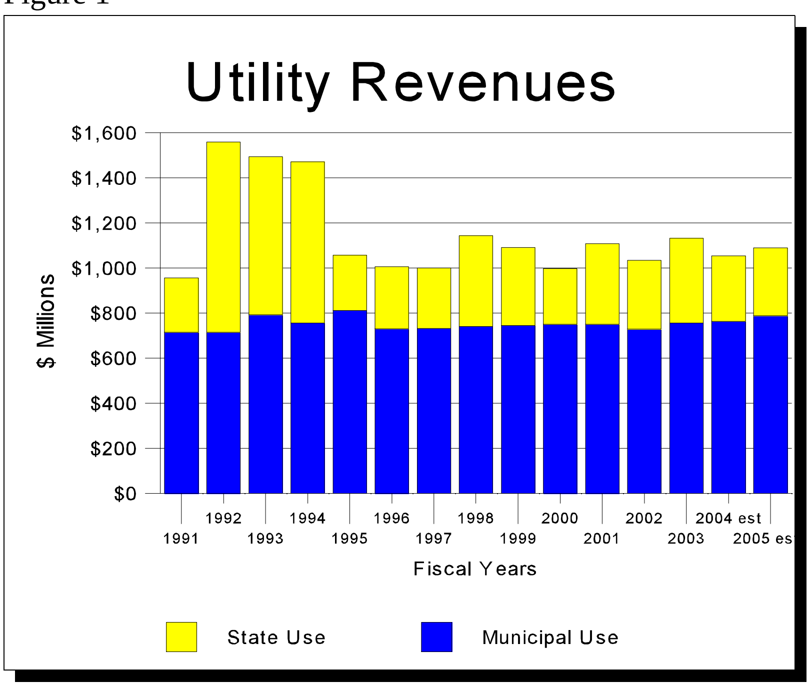
Fiscal Year 2005 will be the eighth year under the revised system of public utility, energy and telecommunications taxation. P.L.1997, c.162 repealed the 1940 State tax system of franchise and gross receipts taxes imposed on regulated gas and electric utilities and telecommunications utilities operating in New Jersey, effective on January 1, 1998. Energy utilities are now subject to the sales and use tax, the corporation business tax (CBT) and the transitional energy facility assessment tax (TEFA), a tax intended to phase out over time. Telecommunications utilities became subject to the CBT under this act.

Figure 1 below displays public utility revenues between FY 1991 and FY 2005. The revenues are divided into two categories: Municipal Use, which is "off budget" and State Use, which is "on budget." Collections through FY 1997 were under the old public utility tax system. The State Use portions from FY 1992 to FY 1994 included substantial scheduled prepayments from large utilities pursuant to statutory changes at that time. Since FY 1998 taxes have been collected under the current law. Figures 2 through 5 display the actual and anticipated revenues from the replacement taxes between FY 2002 and FY 2005 in greater detail.

P.L. 1997, c.167 replaced the complex aid distribution formulae that had been contained in the franchise and gross receipts statutes and provided a new system for the distribution of State aid to municipalities. In FY 1998, $740 million from the taxes were credited to the Energy Tax Receipts Property Tax Relief Fund and distributed to municipalities according to the new formula. The amount credited to this fund grew to $763 million in FY 2004. For FY 2005, the Executive is estimating the credited amount will grow by $25 million to $788 million.

From a budgeting perspective, the tax revenues credited to the Energy Tax Receipts Property Tax Relief Fund are considered "off budget" and therefore not included in either the anticipated revenues or the amount of State aid appropriated in the annual appropriations act.

Figure 1



The TEFA was originally scheduled to end in FY 2002. However, P.L. 2001, c.433, extended the assessment through FY 2006. For FY 2002 through FY 2004, the 2001 assessment rates were used. The TEFA is scheduled to phase down in FY 2005 and FY 2006, and disappear in FY 2007, under current law. However, the Executive is proposing a further extension of the TEFA at current levels through FY 2007. Those additional amounts are shown in the figures. Legislation is required to implement this proposal.

Figure 2
Actual Public Utility Tax Revenue Fiscal Year 2002
($ Millions)

Revenue Source	On-Budget (State Use)	Off-Budget (Municipal Aid)	Total
Sales and Use Tax		$565.6	$565.6
Corporation Business Tax		$163.2	$163.2
Transitional Energy Facilities Assessment (TEFA)	$221.2	$0.2	$221.4
Customer Specific Tax	$2.0		$2.0
Franchise and Gross Receipts Tax Water and Sewer Utilities	$72.7		$72.7
Public Utility Excise Tax Water and Sewer Utilities	$9.9		$9.9
Total	$305.8	$729.0	$1,034.8

Source: Department of Treasury, March 2003.

Figure 3
Actual Public Utility Tax Revenue Fiscal Year 2003
($ Millions)

Revenue Source	On-Budget (State Use)	Off-Budget (Municipal Aid)	Total
Sales and Use Tax		$670.4	$670.4
Corporation Business Tax	$56.2	$84.6	$140.8
Transitional Energy Facilities Assessment (TEFA)	$233.0		$233.0
Customer Specific Tax	$2.0		$2.0
Franchise and Gross Receipts Tax Water and Sewer Utilities	$76.5		$76.5
Public Utility Excise Tax Water and Sewer Utilities	$9.6		$9.6
Total	$377.3	$755.0	$1,132.3

Source: Department of Treasury, March 2004.

Figure 4 Anticipated Public Utility Tax Revenue Fiscal Year 2004 ($ Millions)			
Revenue Source	On-Budget (State Use)	Off-Budget (Municipal Aid)	Total
Sales and Use Tax		$620.7	$620.7
Corporation Business Tax		$109.1	$109.1
Transitional Energy Facilities Assessment (TEFA)	$211.0	$32.9	$243.9
Customer Specific Tax	$2.0		$2.0
Franchise and Gross Receipts Tax Water and Sewer Utilities	$69.0		$69.0
Public Utility Excise Tax Water and Sewer Utilities	$8.7		$8.7
Total	$290.7	$762.7	$1,053.4
Source: Department of Treasury, March 2004.			

Figure 5 Anticipated Public Utility Tax Revenue Fiscal Year 2005 ($ Millions)			
Revenue Source	On-Budget (State Use)	Off-Budget (Municipal Aid)	Total
Sales and Use Tax		$636.4	$636.4
Corporation Business Tax	$11.2	$151.4	$162.6
Transitional Energy Facilities Assessment (TEFA)	$211.0		$211.0
Customer Specific Tax	$2.0		$2.0
Franchise and Gross Receipts Tax Water and Sewer Utilities	$69.0		$69.0
Public Utility Excise Tax Water and Sewer Utilities	$8.7		$8.7
Total	$301.9	$787.8	$1,089.7
Source: Department of Treasury, March 2004.			

Income Tax Snapshots: Tax Years 1988 to 2001

In recent years, New Jersey's gross income tax has become increasingly dependent on the payments of high income taxpayers. In Tax Year (TY) 1988, taxpayers with income below $50,000 paid 33.7 percent of charged tax, while taxpayers with income over $500,000 paid 15 percent of charged tax. By TY 2000, these relative tax burdens were reversed. The lower income group (63% of taxpayers) paid 7.1 percent of charged tax, while the higher income group (the top 1% of taxpayers) paid 37.8 percent of charged tax. Figure 6 displays this pattern over time.

Figure 6

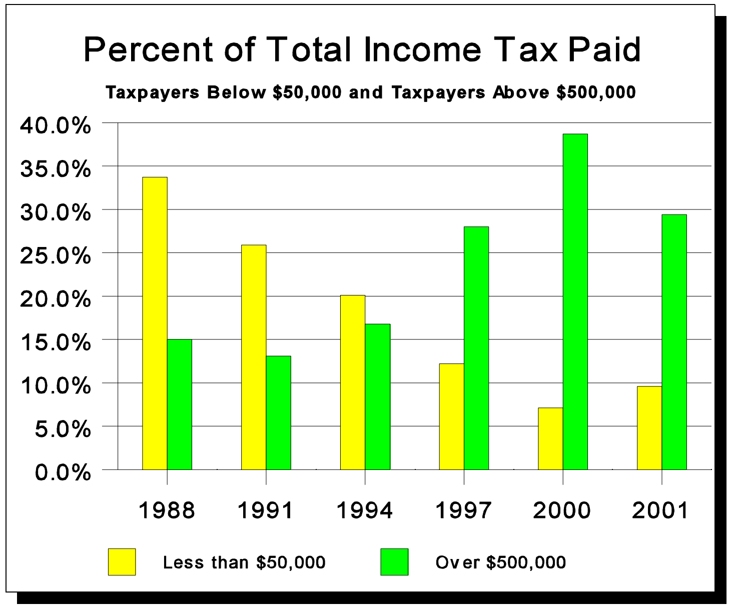


Figure 6 also displays the decline in tax revenue contributions for the top 1% of taxpayers that occurred between TY 2000 and TY 2001, following the stock market collapse. Charged tax from these taxpayers fell to 29.4% of the State total, from $2.5 billion to $1.7 billion. Average income among these taxpayers fell by 13% and the average tax payment fell by 22%. The $800 million drop in tax revenue from the top 1% of taxpayers effectively accounted for the entire drop of State income tax revenue between TY 2000 and TY 2001.

More detailed "snapshots" of the income tax data appear in Figures 7 through 12 on the following pages[1]. The figures represent tax years and do not correspond to any fiscal year because payments and refunds for a single tax year fall into two or more fiscal years. These six income tax snapshots capture a range of circumstances that have occurred since the late 1980's. The figures display moments in time during a period that saw both recession and vigorous growth, the stock market bubble, and upward and downward revisions of tax rates.

The growing dependence on high income taxpayers flows from the tax law changes that enhanced the graduation of marginal tax rates and from the disproportionate growth of non-wage income. During the late 1990's, State tax coffers benefitted because the soaring non-wage income was taxed at higher rates. However, with the drop in stock market values and the concomitant decline in non-wage income, total tax revenues actually fell in FY 2002 and have yet to return to their FY 2001 peak.

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[1] The data come from the NJ *Statistics of Income*, published annually by the Department of the Treasury, and from income tax samples prepared and compiled by the Department of the Treasury's Office of Revenue and Economic Analysis, OREA (formerly the Office of Tax Analysis, OTA).

Figure 7

Tax Year 1988 New Jersey Gross Income Tax Summary

	Less Than $50,000	$50,000 to $100,000	$100,000 to $500,000	$500,000 And Over	All Taxpayers
No. Returns	2,886,971	532,128	139,239	11,205	3,569,543
% of Total	*80.9%*	*14.9%*	*3.9%*	*0.3%*	*100.0%*
Gross Income ($ millions)	$53,385	$35,609	$23,699	$13,351	$126,044
% of Total	*42.4%*	*28.3%*	*18.8%*	*10.6%*	*100.0%*
Avg. Gross Income	$18,492	$66,918	$170,206	$1,191,522	$35,311
Charged Tax ($ millions)	$845	$703	$584	$375	$2,506
% of Total	*33.7%*	*28.1%*	*23.3%*	*15.0%*	*100.0%*
Average Charged Tax	$293	$1,321	$4,191	$33,467	$702

Source: 1988 *Statistics of Income*, Department of Treasury, OTA.

Figure 8

Tax Year 1991 New Jersey Gross Income Tax Summary

	Less Than $50,000	$50,000 to $100,000	$100,000 to $500,000	$500,000 And Over	All Taxpayers
No. Returns	2,832,552	635,613	177,845	7,646	3,653,656
% of Total	*77.5%*	*17.4%*	*4.9%*	*0.2%*	*100.0%*
Gross Income ($ millions)	$50,967	$43,174	$28,583	$8,283	$131,008
% of Total	*38.9%*	*33.0%*	*21.8%*	*6.3%*	*100.0%*
Avg. Gross Income	$17,993	$67,925	$160,719	$1,083,312	$35,857
Charged Tax ($ millions)	$882	$998	$1,084	$447	$3,410
% of Total	*25.9%*	*29.3%*	*31.8%*	*13.1%*	*100.0%*
Average Charged Tax	$311	$1,569	$6,095	$58,462	$933

Source: *Statistics of Income* tax sample, Department of Treasury, OTA, 1998.

Figure 9

Tax Year 1994 New Jersey Gross Income Tax Summary					
	Less Than $50,000	$50,000 to $100,000	$100,000 to $500,000	$500,000 And Over	All Taxpayers
No. Returns	2,581,364	702,383	244,612	11,021	3,539,380
% of Total	*72.9%*	*19.8%*	*6.9%*	*0.3%*	*100.0%*
Gross Income ($ millions)	$47,605	$48,564	$38,930	$13,051	$148,150
% of Total	*32.1%*	*32.8%*	*26.3%*	*8.8%*	*100.0%*
Avg. Gross Income	$18,442	$69,142	$159,150	$1,184,194	$41,858
Charged Tax ($ millions)	$788	$1,090	$1,385	$658	$3,921
% of Total	*20.1%*	*27.8%*	*35.3%*	*16.8%*	*100.0%*
Average Charged Tax	$305	$1,552	$5,662	$59,704	$1,108

Source: *Statistics of Income* tax sample, Department of Treasury, OTA, 1998.

Figure 10

Tax Year 1997 New Jersey Gross Income Tax Summary					
	Less Than $50,000	$50,000 to $100,000	$100,000 to $500,000	$500,000 And Over	All Taxpayers
No. Returns	2,307,759	748,043	341,219	19,820	3,416,841
% of Total	*67.5%*	*21.9%*	*10.0%*	*0.6%*	*100.0%*
Gross Income ($ millions)	$45,959	$52,561	$56,451	$26,636	$181,608
% of Total	*25.3%*	*28.9%*	*31.1%*	*14.7%*	*100.0%*
Avg. Gross Income	$19,915	$70,265	$165,439	$1,343,910	$53,151
Charged Tax ($ millions)	$539	$894	$1,734	$1,234	$4,401
% of Total	*12.2%*	*20.3%*	*39.4%*	*28.0%*	*100.0%*
Average Charged Tax	$233	$1,195	$5,082	$62,270	$1,288

Source: *Statistics of Income* tax sample, Department of Treasury, OREA, March 1999.

Figure 11

Tax Year 2000 New Jersey Gross Income Tax Summary

	Less Than $50,000	$50,000 to $100,000	$100,000 to $500,000	$500,000 And Over	All Taxpayers
No. Returns	2,177,733	784,183	485,268	32,906	3,480,090
% of Total	*62.6%*	*22.5%*	*13.9%*	*0.9%*	*100.0%*
Gross Income ($ millions)	$44,230	$55,899	$82,066	$53,568	$235,763
% of Total	*18.8%*	*23.7%*	*34.8%*	*22.7%*	*100.0%*
Avg. Gross Income	$20,310	$71,283	$169,115	$1,627,916	$67,746
Charged Tax ($ millions)	$465	$968	$2,566	$2,527	$6,526
% of Total	*7.1%*	*14.8%*	*39.3%*	*38.7%*	*100.0%*
Average Charged Tax	$214	$1,234	$5,288	$76,788	$1,875

Source: *Statistics of Income*, Department of Treasury, OREA, 2002.

Figure 12

Tax Year 2001 New Jersey Gross Income Tax Summary

	Less Than $50,000	$50,000 to $100,000	$100,000 to $500,000	$500,000 And Over	All Taxpayers
No. Returns	2,282,600	754,400	436,600	28,100	3,501,700
% of Total	*65.2%*	*21.5%*	*12.5%*	*0.8%*	*100.0%*
Gross Income ($ millions)	$50,177	$58,457	$78,007	$39,736	$226,377
% of Total	*22.2%*	*25.8%*	*34.5%*	*17.6%*	*100.0%*
Avg. Gross Income	$21,982	$77,488	$178,670	$1,414,096	$64,648
Charged Tax ($ millions)	$550	$1,072	$2,431	$1,689	$5,742
% of Total	*9.6%*	*18.7%*	*42.3%*	*29.4%*	*100.0%*
Average Charged Tax	$241	$1,420	$5,569	$60,117	$1,640

Source: *Statistics of Income*, Department of Treasury, OREA, 2003.
http://www.state.nj.us/treasury/taxation/pdf/pubs/soi_tables2001.pdf

New Jersey Review and Economic Outlook for 2004-2005

State of New Jersey
Council of Economic Advisors
February 2004

The Office of Legislative Services thanks the Council for permitting the reproduction of its annual economic report in the following appendix pages of the FY 2004-2005 Revenue Analysis.

NJ Review & Economic Outlook for 2004-2005

Forecast Summary: "The missing cylinder of employment growth has finally started firing in the national economic engine, and New Jersey, with its head start in 2003, will register solid growth in jobs, income, and retail sales in 2004." ***Joseph J. Seneca, Chairman***

NJ Forecast 2004-05

Last year was a transition year for the New Jersey economy. The State posted a fragile 1st half, but there were a growing number of positive indicators by year-end. For 2004, an expanding national economy and recovery in surrounding metropolitan markets provide the backdrop for a New Jersey economy expected to have its best growth since 2000.

	2004	2005
Gross State Product (current $)	**5.0%**	**5.5%**
Personal Income (current $)	**4.5%**	**4.7%**
Non-Ag Employment	**1.4%**	**1.4%**
Retail Sales (current $)	**4.5%**	**4.7%**
Consumer Price Index	**2.0%**	**2.3%**

The NJ outlook continues to benefit from the federal tax cuts enacted last year that boost high-income states like New Jersey. More favorable business depreciation rates and lower taxes on dividends and capital gains enhance disposable income for both businesses and individuals. Total employment in New Jersey posted modest job gains last year and the State's unemployment rate fell and is below the national average. For 2004 and 2005 NJ has an increasing number of sectors that are showing employment growth. Travel and tourism continues to improve while Atlantic City benefits from another round of casino/hotel investment.

High technology is beginning to show renewed signs of life, especially employment in information technologies, which has stabilized and is expected to improve this year. The climate for residential construction remains favorable and should assist markets for materials and supplies, furnishings and fixtures. Increased outlays for national defense and homeland security extend the markets for defense contracting in a wide range of high technology and traditional industries in New Jersey. And, NJ's export markets continue to experience modestly improved demand conditions.

Lastly, growing signs of improvement in the New York City economy will provide spillover impacts to New Jersey service and supply businesses.

While the evidence for accelerated growth in 2004 and 2005 is substantial, there remain areas of concern and weakness in the local economy. Local inflation is higher than the US average - housing price increases exceed national rates. Also, health care costs are rising, and energy prices are up. The cumulative impact of a rising cost of doing business holds back capital investment and business relocations to New Jersey.

Moreover, even with an improved overall outlook and labor market, non-residential construction remains burdened by high office vacancy rates that are expected to be with us for at least two more years. Finally, manufacturing across the country will continue turning to foreign outsourcing and other labor-cost saving measures in a relentless effort to boost productivity and profitability.

The US Economy

After emerging from the 2001 recession, the US economy has registered nine consecutive quarters of growth in real Gross Domestic Product (GDP). GDP grew by 3.1% in 2003, fueled by a strong second half when growth rocketed ahead by 8.2% in the 3rd quarter (a twenty year high) and registered a solid 4% gain in the 4th quarter.

Particularly noteworthy has been the recovery in business investment spending, which grew by 5.2% in 2003 and provided a much-needed boost to the technology sector. International trade also began adding to growth as the depreciated dollar stimulated a 19% rise in exports for the 4th quarter. The tireless U.S. consumer, helped by record low interest rates and tax cuts, continued to support growth, and consumption expenditures increased by 3.1% in 2003. Inflation remained low with the Consumer Price Index (CPI) rising 1.9% (Dec to Dec) and the core rate (without food and energy) increased only by 1.1% (the lowest rate in 43 years). Productivity (output per unit of labor input) soared by 9.4% in the 3rd quarter and grew by a strong 4.2% for the entire year.

Employment, unfortunately, has lagged in this improving economy - indeed the total number of jobs in the nation actually declined throughout this recovery. In 2003, payroll employment fell through August (by 282,000 jobs) and then recovered through December. For the year as a whole, the U.S. economy lost 53,000 jobs. However, payroll employment expanded by 112,000 jobs in January 2004 and although that is still only a modest increase, there is a broad consensus that the national labor markets will continue to improve in 2004.

Across The States

How widespread is the economic recovery? Compared to a year ago, the unemployment rate has fallen in 29 states while 14 states reported a higher jobless rate and 7 states had no change. Non-ag employment posted year over year gains in 26 states.

By sector, the broadest gains were realized in education and health services with increased jobs in 36 states and losses in 14 states. Construction gained in 31 states, bolstered by residential building. The leisure and hospitality sector increased in 29 states reflecting continued improvements in travel and tourism. The finance sector also posted employment gains in more than half the states.

States Reporting Employment Gains/Losses (No.)
November versus year ago

	Increase	Loss/no Chg
Total Non-Ag Employment	26	24
Educ & Health	36	14
Construction	31	19
Leisure & Hospitality	29	21
Finance	27	23
Prof & Bus. Services	23	27
Government	21	29
Manufacturing	0	50

Professional and business services, which includes computer and data processing services and other above average wage services, increased in 23 states, slightly better than gains in 20 states reported at mid-year. Government employment added jobs in only 21 states, with 29 states reporting no change or a decline. Recovery in manufacturing employment remained elusive with year over year losses in all states.

NJ Employment

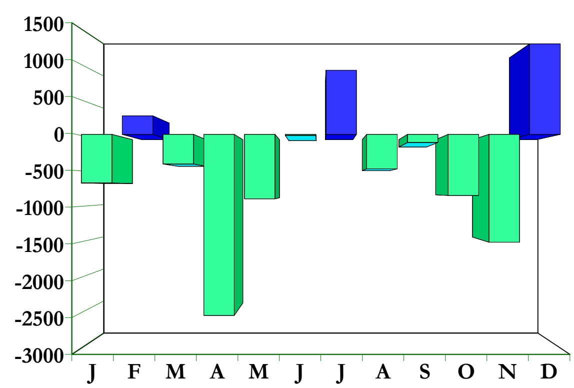
<NOTE: The Council notes that current payroll employment data are subject to an annual 'benchmarking' process by the US Department of Labor that corrects monthly survey employment to the larger universe of NJ employers. This national benchmarking process, applicable to all states, often changes the level of reported job gains in the previous year or two. This year's benchmarking may result in significant changes in NJ's historic employment data because of technical issues, but should not alter the improved 2004-2005 employment outlook>

Nationally, soaring improvements in labor productivity last year limited the number of new hires. Although we lack comparable data at the state level, it is likely that large productivity gains hindered job creation in NJ as well, resulting in an average annual reported gain of almost 17,000 jobs. The State's average unemployment rate for all of 2003 at 5.7% remained below the national rate of 6% and lower than the 8.2% rate in New York City and the 7.7% jobless rate in Philadelphia.

Although NJ's average annual job gains were modest last year, the State finished the 2nd half of 2003 with 5 months of declining unemployment, and 8 consecutive months of year-over-year gains in payroll employment.

Other positive labor market indicators include fewer initial claims for unemployment insurance that, versus a year ago, were lower in 9 of the past 12 months

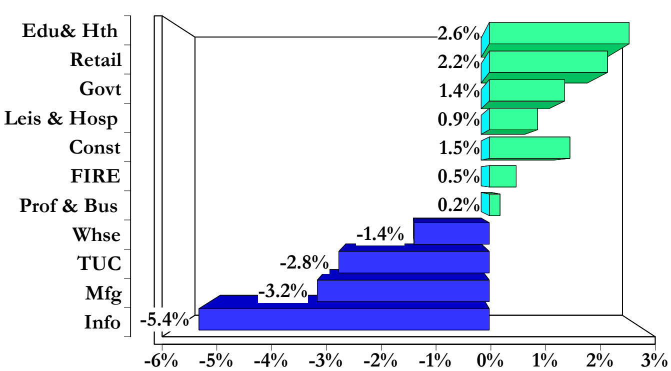
NJ Initial Unemployment Claims
Year over year changes



The temporary help personnel supply businesses, often an indicator of future hiring trends, expanded last year. Temporary help employment expanded in 11 of the previous 12 months, ending the year with a 2.4% increase in employment.

Looking back, sectors that contributed to employment gains were led by education & health services (+2.6%) which is driven more by demographics than the business cycle. Retail trade (+2.2%) and leisure & hospitality services (+.9%) benefited from increased consumer spending and improvements in the travel and tourism sector. Local government hiring boosted total government employment by 1.4%. Another strong year for home building and an expanding school construction program generated 1.5% more construction jobs. Lastly, modest gains were observed in the high wage service sectors of finance (+.5%) and business services (+.2%)

NJ Payroll Employment Change, 2002-03



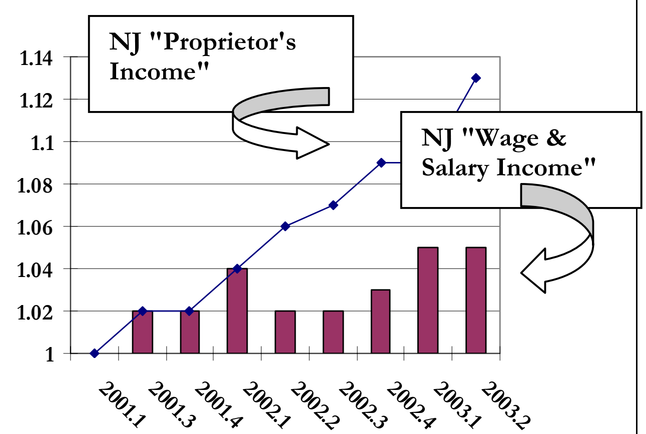
Lagging sectors were led by information technologies, manufacturing, and transportation/logistics. Factory employment, following national trends, declined by 3.2% related to weak capital spending, stagnation in hi-tech investment, and highly competitive overseas markets. Information technology dropped by 5.4%, while Transportation, communication and utilities (which includes logistics wholesale trade and warehousing) declined by 2.8%.

The Jobless Recovery?

The national recovery is more than 27 months old and many indicators have posted strong year-over-year gains. Employment, however, continues to lag. But is the job market as weak as the current data suggest?

There are two sources of US labor market statistics - one survey asks employers how many workers they have, while the second survey calls people at home and asks a series of work-related questions. The surveys have given opposite results at the national level. In New Jersey, both point to job growth, but the household survey has registered many more new jobs. The payroll survey does not easily measure self-employment. Could rising self-employment be the missing link underlying a weak labor market as measured by the payroll survey?

Evidence of rising self-employment is reflected in the recent growth observed in the amount of income earned by the self-employed (proprietors). Buried within the NJ personal income statistics are line items reporting income earned by proprietors. For the past two years proprietors' income grew at the annual rate of 5.2%, while traditional wage and salary income increased at the annual rate of (only) 1.9%.



The growth in proprietors' income may be from improving income for the self-employed, increased entrepreneurial activity in New Jersey, or from corporate outsourcing of more assignments to former employees now serving as consultants.

Whatever the underlying causes, proprietors' income is growing rapidly and is claiming a larger share of NJ personal income. The latest income data show proprietors' income in NJ now exceeds total wages and salaries earned in the state's manufacturing sector.

Personal Income & Retail Spending

NJ personal income for 2003 was recently revised to 2.9% versus the national 3.2% increase. Despite an improving labor market, the State's income gains were limited by modest increases in wages paid to workers and lower returns on investment incomes. For 2004, personal income is expected to rise 4.5%.

New Jersey's retail/consumer markets will benefit from continuing growth in payroll employment, gains in wage & salary payments, and a continuing recovery in travel and tourism. Consumer spending will receive an additional boost from upper income households who are due sizeable tax refunds in 2004 resulting from the 2003 federal tax cuts in capital gains and dividends. The Outlook expects consumer spending to rise by 4.5% in 2004 and 4.7% in 2005, up from an estimated 2.5% gain in 2003.

In 2003, NJ's consumer markets mirrored the small improvements in local labor markets as households started to recover from the financial burdens of the 2001 recession. Personal bankruptcies have fallen to a pre-recession level, while business bankruptcies peaked last year and are now declining.

Last year's 2.5% gain in consumer spending triggered a rise in retail jobs of almost 2%, making retail trade one of the best job creating sectors of 2003.

Key indicators of the health of retail markets are new car sales, home sales, and new residential building. Despite a flood of dealer incentives, motor vehicle registrations dropped by 1.9% from a year earlier. This was the 3rd consecutive year of declining registrations. With a recovery well under way in 2004, we anticipate a modest rebound in motor vehicle sales (2.7%).

Sales of existing homes (over 140,000) in 2003 remained at a high level, up 6% from 2001. Meanwhile, new residential building permits again exceeded 30,000 units. With near term prospects for continued low interest rates and improving demand conditions, NJ's residential markets for both new and existing homes will continue to generate strong downstream spending on home renovations, furnishings, appliances and fixtures.

Tourism contributed to significant retail trade increases last year based on Atlantic City visitor data and casino performance figures.

For 2004 and 2005 consumer market activity appears poised for growth. However, consumer spending remains exposed to a number of risks including rising interest rates, the future performance of the stock market and its resulting impact on household wealth and spending, and concerns over homeland security and its effect on a recovering travel and entertainment sector.

Consumer Prices

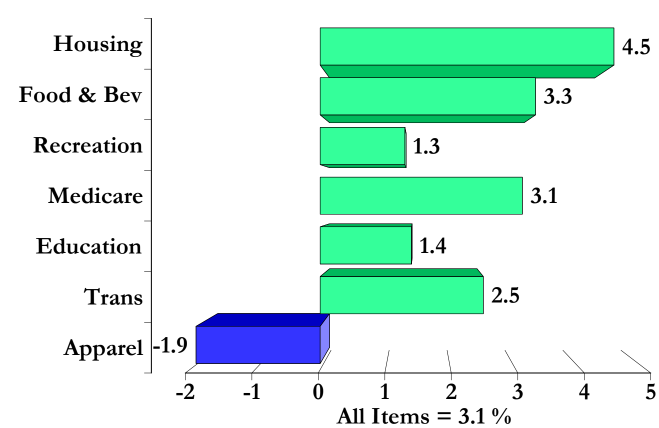
Inflation has bottomed out, and with continuing slack in the regional economy, prices are not expected to accelerate in 2004. Consumer prices in the New York/New Jersey metropolitan area rose by 3.1% in 2003 from a year earlier average. Nationally, the CPI rose by an annual average of 2.4%.

What caused consumer prices to rise? Housing and energy were the two major contributors to regional price increases. Energy/utility prices rose 9.2% and housing costs rose an average of 4.5% for the year. Across the nation the CPI housing component rose only 2.7%.

In 2003 consumer prices were driven higher by energy, housing and medical services. Cumulatively these items account for about 40% of consumer spending. Below average price increase were observed for transportation with a +2.5% increase), education & communications (+1.4%), recreation (+1.3%), apparel (-1.9%).

For 2004 the NY/NJ CPI is expected to post a smaller increase (+2%) as local housing markets, and home prices are expected to moderate and energy prices are expected to stabilize.

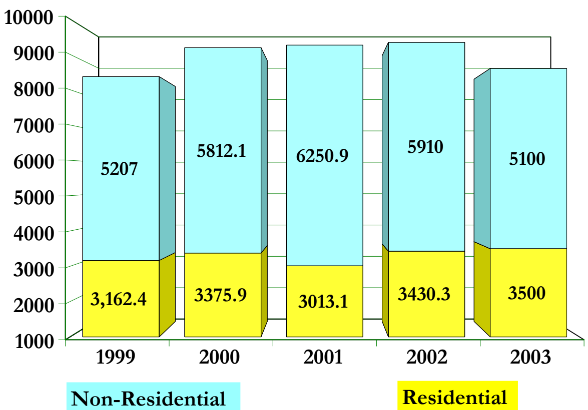
NY/NJ Consumer Price Index, Percent Change, 2002-03



Investing in NJ

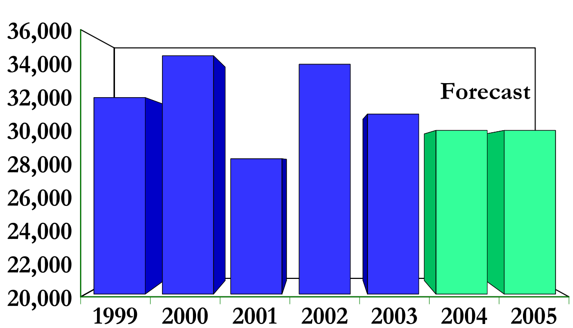
Building and construction activity typically reaches a peak late in the business cycle and recovers well after the recession trough has passed. The year 2003 was no exception to this pattern. Construction contracts will be down about 8% from a year earlier and total $8.5 billion. Construction market performance was the result of a healthy home building segment (about 40% of total construction), and a weak non-residential segment (about 60%).

NJ Construction Contracts (Millions $)
Residential + Non-Residential



Residential construction (approx $3.5 billion) should conclude 2003 with a 5% to 6% gain over last year. The increase in residential investment resulted largely from the rising value of home construction (larger, more expensive dwellings) and from the increase in housing starts (based on the 20% increase in building permits in the prior year).

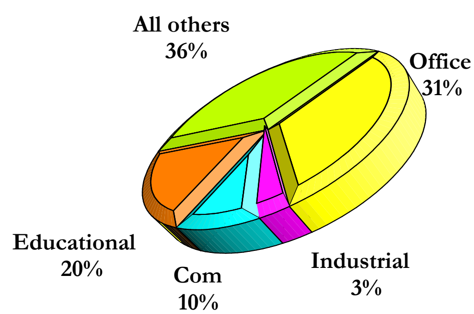
NJ Residential Building Permits



Building permits fell almost 9% in 2003 suggesting that housing starts should moderate in 2004. With general economic conditions favorable to home building and home sales, NJ's residential markets should extend their gains through 2005 with rising home values driving 5% annual increases in construction contracts.

The non-residential construction market fell by almost 13% in 2003, constrained by a drop of 20% in commercial and industrial building and a 15% decline in office construction. The best performing non-residential segment was education building with a gain of 13% in 2003. The NJ school rebuilding program accelerated last year and added over $100 million in construction to year earlier totals. The school building segment now accounts for 20% of NJ's non-residential construction activity and was a major boost to the State's economy.

NJ Non-Residential Construction, 2003
Percent Distribution



The recession, corporate downsizing, and the return of pre-leased office space to the market drove the State's office vacancy rate to about 15% in 2003. Office building, the largest non-residential segment, will gradually recover as office job creation accelerates in 2004 and 2005. Based on current rules of thumb, the office vacancy rate falls 1 percentage point for each additional 10,000 office jobs. Over the next two years construction activity will begin to transition from residential to non-residential building as the recovery matures. This transition will have implications for material suppliers since these two construction sectors use a different mix of materials, furnishings, and fixtures.

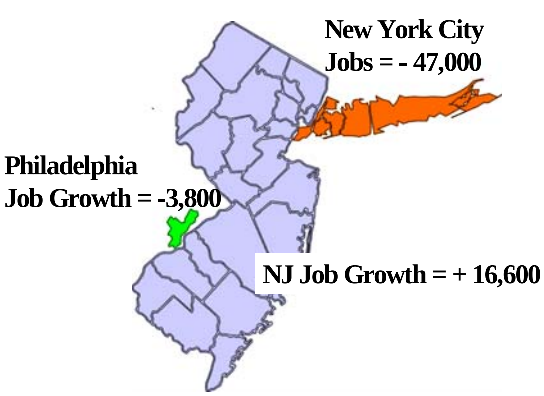
International Trade

NJ exports are expected to contribute little to overall economic growth in 2004. Following a 10% decline in 2002, NJ exports declined 1.5% in 2003. In contrast, US exports increased 4.4% in 2003. Nationally export growth began to accelerate late in 2003 with shipments of capital goods and industrial supplies; goods that are not widely produced in New Jersey. The US recovery provides evidence that manufacturers are benefiting from stronger growth in world demand and the weaker US dollar. Exports were boosted by service exports, which rose sharply, but the lack of comparable State data does not tell us how this may have benefited NJ.

Most of NJ's export situation is the result of a combination of industry mix and geography. New Jersey produces and exports a high proportion of technology goods. The demand for these goods has been in a recession for more than three years. As global high tech capital spending recovers in 2004, NJ shipments are expected to accelerate. Also, the economies of NJ's largest trading partners (NAFTA - Canada and Mexico and the European Union) were growing slowly, but recent forecasts by the World Bank project faster growth in these export markets. The added effects of more investment in high tech and a weaker US dollar will all contribute to improved New Jersey trade this year and in 2005.

The Region

The regional economic growth pattern has changed little - NJ continued to add jobs while the surrounding metropolitan areas (New York City and Philadelphia) continued to lose employment. For 2003, NJ added, as an annual average, 17,000 jobs, while Philadelphia lost 4,000 jobs and New York City shed 47,000 jobs. As a result New York City led the region in joblessness at 8.2%, Philadelphia trailed at 7.7%, while New Jersey's unemployment rate fell to 5.7%.



Given the sheer size of the New York City (NYC) economy, its prospects significantly affect Northern NJ's businesses and households that service, supply, and work for City-based businesses. On a monthly peak to trough basis, NYC lost 235,000 jobs during its 33-month decline that finally ended in the fall of 2003. Declines in sectors that have strong regional multiplier effects, such as finance, information technologies, and professional & business services have reduced opportunities for numerous NJ based businesses.

Recent indicators suggest that the dual effects of recession and homeland security are slowly dissipating and a NY metropolitan recovery is underway. Foreign tourism also is improving as jobs in the leisure & hospitality sector rose in 2003. Hotel occupancy is improving and air traffic is up from year ago levels. More importantly, employment in the finance sector may have bottomed out and begun to improve. For 2004 and 2005 continued improvements in the finance, media, and tourism sectors are expected. As a result the Council expects economic activity in New Jersey to benefit from a recovering New York City.

The Philadelphia economy offers fewer opportunities to support NJ growth in 2004. Philadelphia continues to lose jobs, albeit at a lesser rate. Manufacturing losses still weaken the City, while service sector growth is not yet sufficient to replace the loss in factory employment.

NJ Labor Markets

Across the State, differences in industry mix accounted for much of the variation in labor market growth. Southern NJ, which includes the State's smallest Labor Markets, gained the most jobs, accounting for one half of NJ's employment gains for the year. The Camden Labor Area contributed the most jobs to Southern NJ's economy last year with increases in retail trade, education & health services, finance, and government. The Atlantic City Labor Area benefited from a continuing recovery in tourism and the mid-year opening of the new Borgata casino. Casinos increased employment by almost 3% while posting their best revenue gains in their 25-year existence.

Northern NJ, accounting for one half of the State's employment, added jobs at a rate comparable to the NJ average of .4%. Weak job prospects in New York City, few or no increases in the finance sector, and across-the-board weakness in manufacturing limited employment increases.

Central NJ finished the year with little change in total employment. Most hi tech sectors, which are heavily concentrated in this area, held job levels constant with year earlier totals.

NJ Review & Economic Outlook: 2004 - 2005

(Current $ or Nos.)	**1999**	**2000**	**2001**	**2002**	**2003**	**Forecast 2004**	**2005**
Gross State Product (bill)	$332.16	$357.45	$365.39	$377.00	$394.00	**413.7**	**436.45**
Personal Income (bill)	$288.80	$318.20	$328.70	$339.89	$349.75	**365.5**	**382.7**
Retail Sales (bill)	$93.6	$101.9	$105.0	$106.7	$109.4	**$114.3**	**$119.7**
New Vehicle Registrations (000's)	611.9	663.6	655.5	645.5	633.0	**650**	**660**
Non-Res. Construction Contracts (mill $)	$5,207.0	$5,812.1	$6,250.9	$ 5,910.0	$ 5,100.0	**$ 5,355.0**	**$ 5,756.0**
Residential Building Permits (No.)	32,004	34,560	28,267	34,044	31,000	**30,000**	**30,000**
Res. Construction Contracts (mill $)	$3,162.4	$3,375.9	$3,013.2	$3,430.3	$3,500.0	**$ 3,675.0**	**$ 3,858.8**
Consumer Price Index (1982-84=100)	177.0	182.5	187.1	191.9	197.8	**201.76**	**206.3**
(Real 1982$)							
Gross State Product (bill)	$187.7	$195.9	$195.3	$196.5	$199.19	**$205.0**	**$211.6**
Personal Income (bill)	$163.2	$174.4	$175.7	$177.1	$176.82	**$181.2**	**$185.5**
Retail Sales (bill)	$52.9	$55.8	$56.1	$55.6	$55.04	**$56.6**	**$58.0**
Non-Res. Construction Contracts (mill $)	$2,941.8	$3,184.7	$3,340.9	$3,079.7	$2,578.4	**$2,654.1**	**$2,790.1**
Res. Construction Contracts (mill $)	$1,786.7	$1,849.8	$1,610.5	$1,787.5	$1,769.5	**$1,821.5**	**$1,870.5**
Employment:							
Total Non-Farm (000)	3,901.1	3,994.5	3,997.2	3,993.8	4,010.4	**4,066.2**	**4,121.3**
Manufacturing (000)	422.5	421.6	401.2	368.8	357.0	**348.07**	**341.1**
Service Producing Industries (000)	2,755.2	2,832.5	2,833.0	2,846.3	2,860.9	**2,915.9**	**2,970.7**
Government	577.6	588.8	602.6	615.2	623.3	**626.01**	**635.25**
Unemployment Rate (%)	4.6%	3.7%	4.2%	5.8%	5.8%	**5.7%**	**5.6%**

Percent Change from previous year:	**1999**	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**
Gross State Product (Current $, bill)	4.8%	7.6%	2.2%	3.2%	4.5%	**5.0%**	**5.5%**
Personal Income (Current $, bill)	3.6%	10.2%	3.3%	3.4%	2.9%	**4.5%**	**4.7%**
Retail Sales (Current $, bill)	9.3%	8.9%	3.0%	1.6%	2.5%	**4.5%**	**4.7%**
New Vehicle Registrations	11.1%	8.4%	-1.2%	-1.5%	-1.9%	**2.7%**	**1.5%**
Non-Res. Construction Contracts	23.1%	11.6%	7.5%	-5.5%	-13.7%	**5.0%**	**7.5%**
Residential Building Permits (No.)	2.1%	8.0%	-18.2%	20.4%	-8.9%	**-3.2%**	**0.0%**
Res. Construction Contracts		6.8%	-10.7%	13.8%	2.0%	**5.0%**	**5.0%**
Consumer Price Index (All Urban)	2.0%	3.1%	2.5%	2.6%	3.1%	**2.0%**	**2.3%**
Gross State Product (82$, bill)	2.8%	4.4%	-0.3%	0.6%	1.4%	**2.9%**	**3.2%**
Personal Income (82$, bill)	1.6%	6.9%	0.8%	0.8%	-0.2%	**2.4%**	**2.4%**
Retail Sales (82$, bill)	7.2%	5.6%	0.5%	-0.9%	-1.0%	**2.9%**	**2.4%**
Non-Res. Construction Contracts (82$)	20.7%	8.3%	4.9%	-7.8%	-16.3%	**2.9%**	**5.1%**
Res. Construction Contracts		3.5%	-12.9%	11.0%	-1.0%	**2.9%**	**2.7%**
Employment:							
Total Non-Farm	2.6%	2.39%	0.07%	-0.1%	0.4%	**1.4%**	**1.4%**
Manufacturing	-11.6%	-0.2%	-4.8%	-8.1%	-3.2%	**-2.5%**	**-2.0%**
Service Producing Industries	5.3%	2.8%	0.0%	0.5%	0.5%	**1.9%**	**1.9%**
Government	1.0%	1.9%	2.3%	2.1%	1.32%	**0.4%**	**1.5%**

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