

**Remarks of David J. Rosen**  
**Legislative Budget and Finance Officer**  
**To the Senate Budget and Appropriations Committee**  
**May 18, 2011**

When we appeared before you in March, we noted the small difference between the OLS revenue forecast and the revenue projections contained in the Governor's Budget Message (GBM). But I added:

*The real question ought not be whether OLS or the Executive is more accurate in their current forecasts --- but rather whether the similar pictures we paint are accurate. The hardest thing in revenue forecasting is the accurate anticipation of the turns or pivots in the economy.*

At that time I discussed two revenue sources about which we had real forecasting concerns. About the corporation business tax, I said:

*A significant rebound this year is likely given [the] low base [last April]and national reports of improved corporate profits. OLS' forecast is slightly more cautious than the Executive's, but would also require significant growth and a return to a strong fourth quarter. We are both banking on the CBT reaching a turning point this Spring; a turning point which is not yet clearly visible in the data.*

And when discussing the gross income tax, I noted that our annual concern about an April surprise was compounded by uncertainty about the effect of tax rate changes and mixed economic signals.

While each of these warnings proved appropriate, the net impact on the State's resources is distinctly positive.

The corporation business tax did not experience the turnaround that was anticipated in April – neither in New Jersey nor elsewhere - - and we are reducing our forecast for the CBT in both FY2011 and FY2012. In

the current year we are projecting \$2.202 billion - \$190 million less than in the GBM and for FY2012 we now anticipate \$2.330 billion, \$253 million less than the GBM.

This loss of \$443 million is more than offset by a remarkable development for the gross income tax. In a pattern that was evident in Washington and in the capitals of our sister states, April income tax payments for tax year 2010 far exceeded expectations. As a result we have increased our income tax forecast to \$10.710 billion this year - \$634 million above GBM – and \$11.340 billion - - \$812 million above GBM - - in FY2012.

<b>Fiscal Year 2011 Revenue Estimates</b>			
<b>(\$ millions)</b>			
	<b><u>GBM</u></b>	<b><u>OLS (May)</u></b>	<b><u>Difference</u></b>
Gross Income Tax (GIT)	\$10,076.1	\$10,710.0	\$633.9
Sales Tax*	8,208.3	8,219.4	\$11.1
Corporation Business Tax*	2,391.9	2,201.8	-\$190.1
Other Revenues	7,585.8	7,560.5	-\$25.3
<b>Grand Total, All Funds</b>	<b>\$28,262.1</b>	<b>\$28,691.7</b>	<b>\$429.6</b>
GBM = Governor's Budget Message. * Energy revenues included.			
<b>Fiscal Year 2012 Revenue Estimates</b>			
<b>(\$ millions)</b>			
	<b><u>GBM</u></b>	<b><u>OLS (May)</u></b>	<b><u>Difference</u></b>
Gross Income Tax (GIT)	\$10,528.3	\$11,340.0	\$811.7
Sales Tax*	8,542.6	8,521.4	-21.2
Corporation Business Tax*	2,582.2	2,329.7	-252.5
Other Revenues	7,721.0	7,666.8	-54.2
<b>Grand Total, All Funds</b>	<b>\$29,374.1</b>	<b>\$29,857.9</b>	<b>\$483.8</b>
GBM = Governor's Budget Message. * Energy revenues included.			

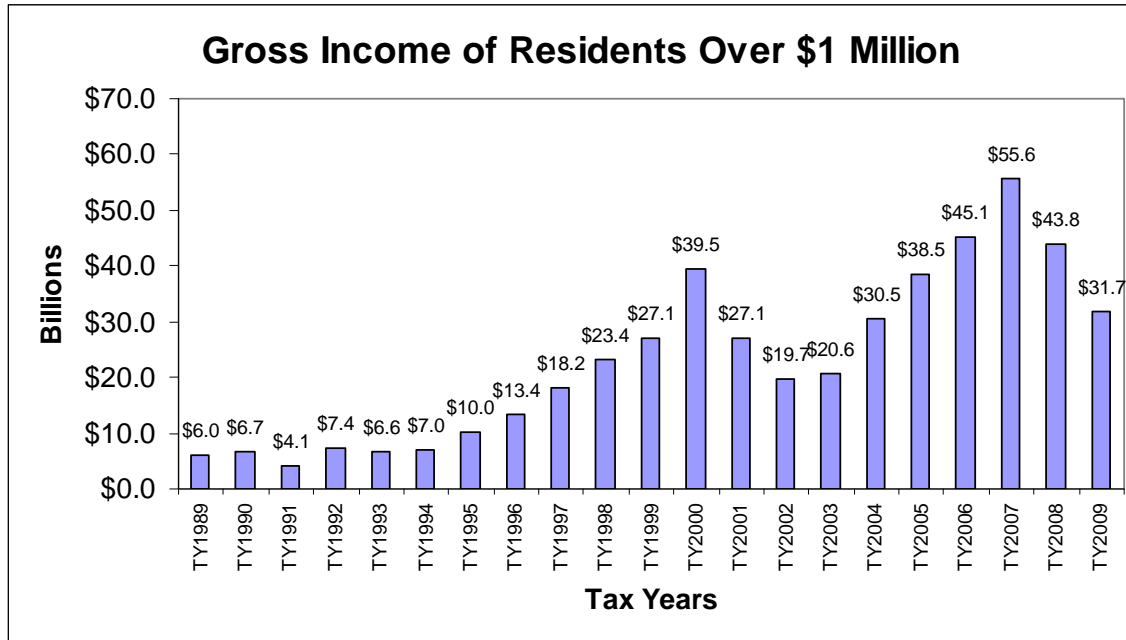
To summarize, over the two years we expect \$1.446 billion more from the income tax and \$443 million less from the corporation business tax than was anticipated in the GBM. A number of smaller differences –

more down than up - - produce a total two year forecast from OLS that is \$914 million higher than the GBM. (A more detailed set of revenue tables which includes a comparison with the Treasurer's revised estimates is attached to this statement.)

So what happened?

As we have noted in the past, the corporation business tax is the hardest revenue to forecast. As was shown this year there is often little correlation between corporate profits that are reported publicly and the profits on which corporations have a tax liability. There are so many avenues by which corporations can shift and reduce tax liabilities that one commentator has referred to it as a voluntary tax.

I believe we have a clearer explanation for the gross income tax surge. Just after we appeared here in March we received some detailed information on TY 2009 tax payments, showing marked declines for high income taxpayers. Between TY 2007 and TY 2009 the number of returns reporting \$1 million of income declined by 33% and the income reported on those returns declined by 43%. And, despite the one-year tax rate increases applicable to that year, the tax liability of those taxpayers declined by 37%.

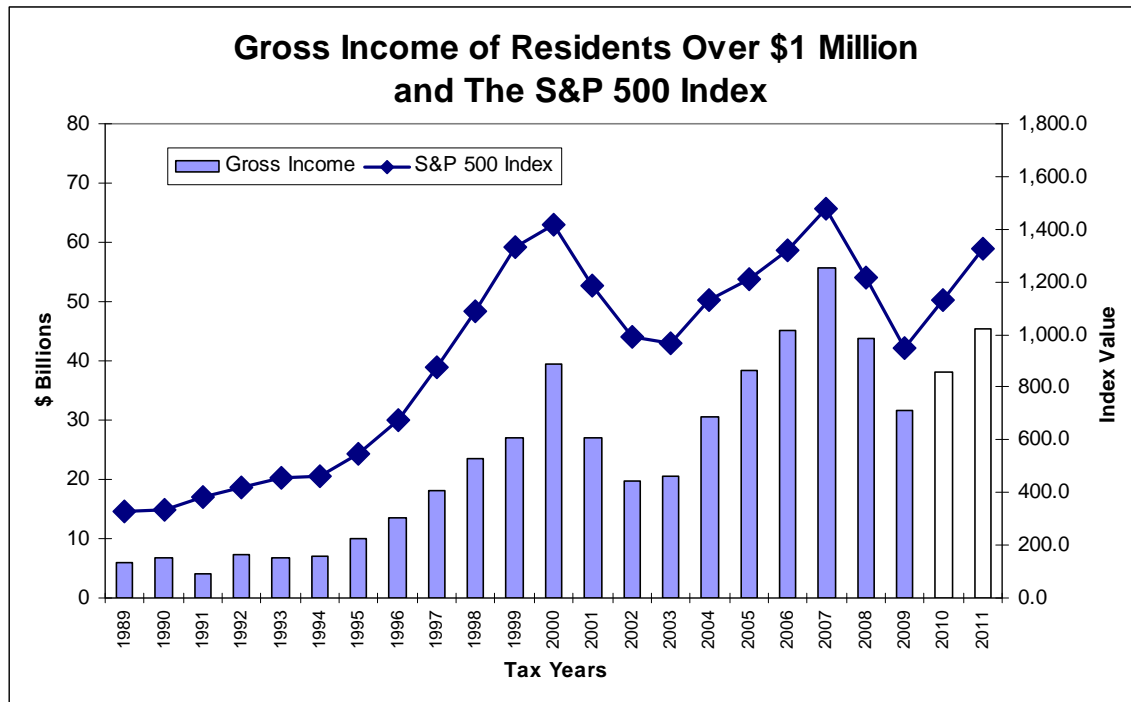


What is clear to us now, but was less clear back in March, is the extent to which the collapse of the income tax during this recession was focused at the high end. Between 2007 and 2009 the total charged tax for all resident taxpayers declined by \$1.7 billion. Of this amount, \$1.3 billion was a decline in tax liability for people with incomes over \$1 million. In contrast, taxpayers below \$500,000 accounted for only \$228 million of the decline.

The takeaway from these facts is that while the recession has had terrible consequences for many middle and lower income New Jersey residents, it was the loss of income for wealthier New Jerseyans that sunk our income tax collections.

We knew that the wealthiest one-half of one percent who pay about one-third of the income tax were important, but we had not anticipated that their fortunes would account for more than three-quarters of the revenue decline.

And it is the flip side of that coin that is appearing in our revenue collections now.



In trying to explain the vigor of the rebound during what appears to be a lackluster economic recovery, we compared the historic pattern of high-end income to the performance of the stock market. The graph included in this testimony illustrates the extraordinarily high degree of association between the S&P 500 Index and the total income on returns reporting at least \$1 million<sup>1</sup>. The bars we added for tax years 2010 and 2011 are estimates based on the statistical relationship<sup>2</sup>. The 2010 bar is consistent with the revenue windfall we received last month.

It is difficult to look at this graph and not conclude that the performance of the stock market is the factor which drives the volatility of our income tax. If a picture is worth a thousand words, this graph may be worth a billion dollars.

<sup>1</sup> The correlation coefficient is 0.92 and the r-squared is 0.85.

<sup>2</sup> The S&P 500 value for each year is the average of the index values on the first day of each month of the year. For 2011, the average is for the first five months of the year.

As the members of this committee work to craft the Fiscal Year 2012 appropriations act over the next six weeks, the staff of the Office of Legislative Services stands ready to provide whatever assistance you may require. For now, we would be pleased to answer your questions.

Figure A  
**Revised Fiscal Year 2011 Revenue Estimates -- May 2011**

Millions of \$

Revenue Source	<u>Executive</u>	<u>Executive</u>	<u>Executive</u>	<u>OLS Revised</u>	<u>Difference</u>	
	<u>Estimates</u> February 2011	<u>Exec Revised</u> May 2011	<u>Change Feb to</u> May	<u>May 2011</u>	<u>OLS May -</u> <u>Exec March</u>	<u>Difference OLS</u> <u>May - Exec May</u>
<b>Major Taxes:</b>						
<b>Sales Tax, Total</b>	<b>\$7,607.3</b>	<b>\$7,614.4</b>	<b>\$7.1</b>	<b>\$7,614.4</b>	<b>\$7.1</b>	<b>\$0.0</b>
<i>Sales Tax, Base</i>	7,775.0	7,847.0	72.0	7,847.0	72.0	0.0
<i>Dedicated Transfer to PTRF</i>	-601.0	-605.0	-4.0	-605.0	-4.0	0.0
<i>Sales Tax, Energy</i>	433.3	372.4	-60.9	372.4	-60.9	0.0
<b>Corporation Business Tax, Total</b>	<b>\$2,391.9</b>	<b>\$2,208.8</b>	<b>-\$183.1</b>	<b>\$2,201.8</b>	<b>-\$190.1</b>	<b>-\$7.0</b>
<i>Corporation Business Tax, Base</i>	2,320.0	2,107.0	-213.0	2,100.0	-220.0	-7.0
<i>Corporation Business Tax, Energy</i>	71.9	101.8	29.9	101.8	29.9	0.0
Inheritance Taxes	628.2	628.2	0.0	630.0	1.8	1.8
Motor Fuels Tax	540.9	525.1	-15.8	530.0	-10.9	4.9
Insurance Premiums Tax	499.0	469.4	-29.6	480.0	-19.0	10.6
Realty Transfer Fee	170.9	170.9	0.0	175.0	4.1	4.1
Motor Vehicle Fees	412.0	412.0	0.0	412.0	0.0	0.0
Cigarette Tax	200.6	214.0	13.4	213.0	12.4	-1.0
Petroleum Products Gross Receipts Tax	220.0	219.0	-1.0	215.0	-5.0	-4.0
Corporation Business - Banks and Financial	198.9	173.4	-25.5	180.0	-18.9	6.6
Alcoholic Beverage Excise Tax	88.5	93.4	4.9	93.0	4.5	-0.4
Tobacco Products Wholesale	19.4	19.2	-0.2	19.2	-0.2	0.0
Public Utilities Excise	13.3	13.5	0.2	13.5	0.2	0.0
<b>Subtotal, Major Taxes</b>	<b>\$12,990.9</b>	<b>\$12,761.3</b>	<b>-\$229.6</b>	<b>\$12,776.9</b>	<b>-\$214.0</b>	<b>\$15.6</b>
<b>Misc. Taxes, Fees and Revenues</b>						
Assessment on Property Sold Over \$1 Million	57.5	64.8	7.3	63.0	5.5	-1.8
Transitional Energy Facility Assessment	240.4	243.0	2.6	243.0	2.6	0.0
Public Utility Taxes (State Retention)	100.6	103.0	2.4	103.0	2.4	0.0
Medicaid Uncomp. Care Reimbursement	507.4	507.4	0.0	507.4	0.0	0.0
Good Driver	71.8	71.8	0.0	71.8	0.0	0.0
Hotel Occupancy Tax	65.0	70.0	5.0	70.0	5.0	0.0
Fringe Benefit Recoveries	503.9	494.5	-9.4	494.5	-9.4	0.0
Other	1,061.3	1,066.3	5.0	1,066.3	5.0	0.0
<b>Subtotal, Misc. Revenues</b>	<b>\$2,607.8</b>	<b>\$2,620.7</b>	<b>\$12.9</b>	<b>\$2,618.9</b>	<b>\$11.1</b>	<b>-\$1.8</b>
<b>Interfund Transfers</b>						
State Lottery Fund	930.0	930.0	0.0	930.0	0.0	0.0
Tobacco Settlement/Securitization	54.4	53.9	-0.5	53.9	-0.5	0.0
Other	660.5	655.8	-4.8	655.8	-4.8	0.0
<b>Subtotal, Interfund Transfers</b>	<b>\$1,644.9</b>	<b>\$1,639.6</b>	<b>-\$5.3</b>	<b>\$1,639.6</b>	<b>-\$5.3</b>	<b>\$0.0</b>
<b>TOTAL GENERAL FUND</b>	<b>\$17,243.7</b>	<b>\$17,021.6</b>	<b>-\$222.1</b>	<b>\$17,035.4</b>	<b>-\$208.3</b>	<b>\$13.8</b>
<b>Property Tax Relief Fund (Income Tax)</b>	<b>\$10,076.1</b>	<b>\$10,536.0</b>	<b>\$459.9</b>	<b>\$10,710.0</b>	<b>\$633.9</b>	<b>\$174.0</b>
<i>PTRF Transfer from GF (Sales Tax)</i>	<i>\$618.0</i>	<i>\$622.0</i>	<i>\$4.0</i>	<i>\$622.0</i>	<i>\$4.0</i>	<i>\$0.0</i>
<b>Casino Revenue Fund</b>	<b>\$257.0</b>	<b>\$257.0</b>	<b>\$0.0</b>	<b>\$257.0</b>	<b>\$0.0</b>	<b>\$0.0</b>
<b>Casino Control Fund</b>	<b>\$66.7</b>	<b>\$66.7</b>	<b>\$0.0</b>	<b>\$66.7</b>	<b>\$0.0</b>	<b>\$0.0</b>
<b>Gubernatorial Elections Fund</b>	<b>\$0.7</b>	<b>\$0.7</b>	<b>\$0.0</b>	<b>\$0.7</b>	<b>\$0.0</b>	<b>\$0.0</b>
<b>GRAND TOTAL, ALL FUNDS</b>	<b>\$28,262.1</b>	<b>\$28,504.0</b>	<b>\$241.9</b>	<b>\$28,691.8</b>	<b>\$429.7</b>	<b>\$187.8</b>

Figure B  
**Revised Fiscal Year 2012 Revenue Estimates -- May 2011**  
*Millions of \$*

<u>Revenue Source</u>	<u>February 2010</u> <u>Gov's Budget</u>	<u>Exec Revised</u> <u>May 2011</u>	<u>Executive</u> <u>Change Feb to</u> <u>May</u>	<u>OLS Revised</u> <u>May 2011</u>	<u>Difference OLS</u> <u>May - GBM Feb</u>	<u>Difference OLS</u> <u>May - Exec May</u>
<b>Major Taxes:</b>						
<b>Sales Tax, Total</b>	<b>\$7,917.6</b>	<b>\$7,893.4</b>	<b>-\$24.2</b>	<b>\$7,893.4</b>	<b>-\$24.2</b>	<b>\$0.0</b>
<i>Sales Tax, Base</i>	8,077.5	8,153.0	75.5	8,153.0	75.5	0.0
<i>Dedicated Transfer to PTRF</i>	-625.0	-628.0	-3.0	-628.0	-3.0	0.0
<i>Sales Tax, Energy</i>	465.1	368.4	-96.7	368.4	-96.7	0.0
<b>Corporation Business Tax, Total</b>	<b>\$2,582.2</b>	<b>\$2,340.7</b>	<b>-\$241.5</b>	<b>\$2,329.7</b>	<b>-\$252.5</b>	<b>-\$11.0</b>
<i>Corporation Business Tax, Base</i>	2,429.9	2,261.0	-168.9	2,250.0	-179.9	-11.0
<i>Corporation Business Tax, Energy</i>	152.3	79.7	-72.6	79.7	-72.6	0.0
Inheritance Taxes	666.9	666.9	0.0	680.0	13.1	13.1
Motor Fuels Tax	560.0	535.0	-25.0	530.0	-30.0	-5.0
Insurance Premiums Tax	519.2	499.2	-20.0	500.0	-19.2	0.8
Realty Transfer Fee	191.1	191.1	0.0	192.5	1.4	1.4
Motor Vehicle Fees	492.7	492.7	0.0	492.7	0.0	0.0
Cigarette Tax	202.9	205.5	2.6	213.0	10.1	7.5
Petroleum Products Gross Receipts Tax	223.8	222.8	-1.0	215.0	-8.8	-7.8
Corporation Business - Banks and Financial	221.9	201.9	-20.0	200.0	-21.9	-1.9
Alcoholic Beverage Excise Tax	93.6	93.4	-0.2	97.0	3.4	3.6
Tobacco Products Wholesale	20.9	20.4	-0.5	20.4	-0.5	0.0
Public Utilities Excise	13.3	13.5	0.2	13.5	0.2	0.0
<b>Subtotal, Major Taxes</b>	<b>\$13,706.0</b>	<b>\$13,376.5</b>	<b>-\$329.5</b>	<b>\$13,377.2</b>	<b>-\$328.8</b>	<b>\$0.7</b>
<b>Misc. Taxes, Fees and Revenues</b>						
Assessment on Property Sold Over \$1 Million	64.3	64.3	0.0	70.0	5.8	5.8
Transitional Energy Facility Assessment	177.8	178.7	0.9	178.7	0.9	0.0
Public Utility Taxes (State Retention)	100.6	105.0	4.4	105.0	4.4	0.0
Medicaid Uncomp. Care Reimbursement	441.5	441.5	0.0	441.5	0.0	0.0
Good Driver	71.8	71.8	0.0	71.8	0.0	0.0
Hotel Occupancy Tax	75.0	75.0	0.0	75.0	0.0	0.0
Fringe Benefit Recoveries	496.4	485.8	-10.6	485.8	-10.6	0.0
Other	1,110.2	1,122.5	12.3	1,122.5	12.3	0.0
<b>Subtotal, Misc. Revenues</b>	<b>\$2,537.6</b>	<b>\$2,544.6</b>	<b>\$7.0</b>	<b>\$2,550.3</b>	<b>\$12.8</b>	<b>\$5.8</b>
<b>Interfund Transfers</b>						
State Lottery Fund	1,040.0	1,030.0	-10.0	1,030.0	-10.0	0.0
Tobacco Settlement/Securitization	54.6	54.6	0.0	54.6	0.0	0.0
Other	560.4	555.6	-4.8	555.6	-4.8	0.0
<b>Subtotal, Interfund Transfers</b>	<b>\$1,655.0</b>	<b>\$1,640.2</b>	<b>-\$14.8</b>	<b>\$1,640.2</b>	<b>-\$14.8</b>	<b>\$0.0</b>
<b>TOTAL GENERAL FUND</b>	<b>\$17,898.5</b>	<b>\$17,561.2</b>	<b>-\$337.3</b>	<b>\$17,567.7</b>	<b>-\$330.8</b>	<b>\$6.4</b>
<b>Property Tax Relief Fund (Income Tax), Total</b>						
<i>PTRF Transfer from GF (Sales Tax)</i>	<i>\$10,528.3</i>	<i>\$11,132.0</i>	<i>\$603.7</i>	<i>\$11,340.0</i>	<i>\$811.7</i>	<i>\$208.0</i>
Casino Revenue Fund	\$248.1	\$248.1	\$0.0	\$248.1	\$0.0	\$0.0
Casino Control Fund	\$55.9	\$55.8	-\$0.1	\$55.8	-\$0.1	\$0.0
Gubernatorial Elections Fund	\$0.7	\$0.7	\$0.0	\$0.7	\$0.0	\$0.0
<b>GRAND TOTAL, ALL FUNDS</b>	<b>\$29,374.1</b>	<b>\$29,643.4</b>	<b>\$269.3</b>	<b>\$29,857.8</b>	<b>\$483.8</b>	<b>\$214.4</b>