

Remarks of Frank Haines, Legislative Budget and Finance Officer  
to the Senate Budget and Appropriations Committee  
May 19, 2016

When we appeared before you six weeks ago, we informed you that the OLS revenue forecast for fiscal years 2016 and 2017 was about \$162 million lower than the Executive's over the two fiscal years, a difference of about two-tenths of 1 percent (0.24%). We either agreed or differed minimally with the Executive's forecast for the State's two largest taxes, the Gross Income Tax (GIT) and the Sales and Use Tax, with OLS lower than the Executive. In total, both the Executive and OLS were estimating low growth in FY 2016, in the neighborhood of 2%, followed by improved growth of about 3% in FY 2017. The GIT and the Sales Tax were both seen as the drivers of growth in both years.

With the spring tax filing season largely behind us, both the OLS and the Executive are revising revenues downward. The differences between the OLS and the Executive are not much greater now than they were in April. We are below the Executive for FY 2016 by \$15.3 million, and are \$172.1 million lower in FY 2017, a two-year total of \$187.4 million. That difference is about three-tenths of 1 percent (0.28%).

The OLS is decreasing our forecast for both FY 2016 and FY 2017, by a combined total of about \$868 million compared to our April forecasts, and by about \$1.03 billion below the levels estimated in the Governor's Budget Message (GBM). Figures 1 and 2 show the differences between the GBM and the May OLS forecasts. This comparison is meaningful only to show how the revised OLS outlook would have affected the Executive's original plan presented in February. FY 2016 revenue is now \$617.9 million lower than the GBM estimate, compared to a difference of only \$73.2 million six weeks ago. For FY 2017, our projection is now \$412.2 million lower than the GBM, compared to a difference of just \$88.9 million in April.

We'll get to the more important comparisons between the revised OLS outlook and the Executive's revised outlook shortly. The key point is that while most revenues have performed close to expectations, there is a crucial exception: we were too optimistic about the GIT, and are changing our outlook for both fiscal years. The reduced OLS forecast does not suggest a

significant change in the economy. Consensus economic forecasts project continuing slow growth, and the OLS is also assuming slow growth. The revenue weakness stems from the annual variability of revenue collections.

**Figure 1**

<b>FY 2016 Revenue Estimates</b>			
<i>\$ in Millions</i>			
	<b>Executive Estimate Feb 2016</b>	<b>OLS Revised May 2016</b>	<b>Difference</b>
Gross Income Tax	\$13,758.0	\$13,440.0	-\$318.0
Sales Tax	\$9,315.8	\$9,335.0	\$19.2
Corporation Business Tax	\$2,336.0	\$2,280.0	-\$56.0
All Other Revenues	\$8,391.0	\$8,127.9	-\$263.1
<b>Total Budget Revenues</b>	<b>\$33,800.8</b>	<b>\$33,182.9</b>	<b>-\$617.9</b>

\* May 19, 2016. Includes certain amounts from Treasury's revised revenue forecast.

**Figure 2**

<b>FY 2017 Revenue Estimates</b>			
<i>\$ in Millions</i>			
	<b>Executive Estimate Feb 2016</b>	<b>OLS Revised May 2016</b>	<b>Difference</b>
Gross Income Tax	\$14,424.6	\$13,840.0	-\$584.6
Sales Tax	\$9,597.4	\$9,690.0	\$92.6
Corporation Business Tax	\$2,336.0	\$2,180.0	-\$156.0
<i>Corp. Bus. Tax Treasury Proposal</i>		\$135.0	\$135.0
All Other Revenues	\$8,474.2	\$8,575.0	\$100.8
<b>Total Budget Revenues</b>	<b>\$34,832.2</b>	<b>\$34,420.0</b>	<b>-\$412.2</b>

\* May 19, 2016. Includes certain amounts from Treasury's revised revenue forecast.

I wish to focus now on the GIT, which accounts for most of the forecast revision. Figure 3 displays the performance of the GIT against our expectations in the months of March and April, combined. Overall, the OLS had expected GIT revenues to be flat during these two months, compared to the same two months last year, at \$3.19 billion. As we discussed in the *Tax and Revenue Outlook*, OLS projected growth in final payments of 5%, coming off of 4.8% growth in December and January estimated payments. We also projected 2.5% growth in receipts from withholding of employee wages, based on year-to-date trends at that time. These were modest growth assumptions, in line with recent trends but below historical averages for the GIT. In addition, we anticipated a sharp jump of 16% in refund payments due to the increased earned income tax credit (EITC), and Treasury's accelerated processing of refunds.

**Figure 3**

<b>2016 Gross Income Tax Filing Season</b>					
<b>Tax Revenue and Components in March and April 2016</b>					
<i>\$ in Millions</i>					
	OLS Est.	OLS Est. % Change	Actual	Actual % Change	Difference, Actual v. OLS Est.
Withholding	\$2,011.5	2.5%	\$1,945.7	-0.9%	-\$65.8
Estimated Payments	\$379.8	5.0%	\$349.8	-3.3%	-\$30.0
Final Payments	\$1,961.7	5.0%	\$1,875.8	0.4%	-\$85.9
<u>Less Refunds</u>	<u>-\$1,162.0</u>	<u>16.0%</u>	<u>-\$1,321.0</u>	<u>31.9%</u>	<u>-\$159.0</u>
<b>Total</b>	<b>\$3,191.0</b>	<b>0.0%</b>	<b>\$2,850.3</b>	<b>-10.7%</b>	<b>-\$340.7</b>

Note: March and April estimates as of the OLS Tax and Revenue Outlook report.  
Actual revenues from the Department of the Treasury.

However, actual collections in March and April fell short of our assumptions for each of the four components of the GIT. Despite slow, steady progress in New Jersey employment, withholding collections actually fell 0.9%, \$65.8 million below projections. Estimated payments reversed the December/January growth trend and fell 3.3%, \$30.0 million below projections. Final payments of Tax Year 2015 liabilities -- payments we associate with higher-income taxpayers -- grew by only 0.4%, \$85.9 million below our estimate, and we expect them to decline in May. Refund

payments rose by 31.9%, twice the projected rate and \$159.0 million higher than expected. All told, the GIT's March and April underperformed by a total of \$340.7 million below OLS expectations.

New Jersey is not an outlier in its filing season results. Other states such as California, Massachusetts, Connecticut, and Pennsylvania have reported spring income tax revenues falling short of expectations. Also, the Congressional Budget Office reports that April federal income tax non-withheld receipts (estimated and final payments) were 5% below last April.

While it is too soon to know exactly what is causing these results, the preliminary conclusion is that the weakness seen in spring tax filings reflects the weak stock markets in 2015. The S&P 500 index fell 0.7%, the Dow Jones Industrial Average dropped 2.2%, although the "tech-heavy" Nasdaq index was up 5.7%. For the S&P 500 and the Dow, 2015 was the worst performance since the Great Recession began in 2008. In addition, a leading hedge fund research firm reported that while an estimated 55% of all hedge funds posted gains in 2015, its composite index ended the year down 0.85%. Financial market performance is linked to capital gains, a key source of income for higher-income taxpayers whose quarterly and final tax payments can fluctuate as those gains trend up or down. While the December/January GIT quarterly estimated payments were up 4.8%, it appears that some taxpayers adjusted their initial quarterly payments for 2016 downward in light of lower total liabilities and final payments for 2015.

Given the GIT's recent results, the OLS is reducing its FY 2016 GIT forecast. We are tempering our forecast of estimated payments to a no-growth outlook for the balance of the fiscal year, and are assuming final payments to decrease the rest of FY 2016. In both cases this is a downward revision from 5% growth. We are also scaling back our expectations for withholding payments, but less drastically. We continue to expect that accelerated processing will significantly depress refunds for the remainder of FY 2016, boosting net revenues somewhat. The OLS's revised forecast of \$13.44 billion is \$318.0 million below our previous estimate, and 1.4% above FY 2015, compared to the 3.8% growth rate previously assumed.

The OLS projects modest growth of 3% for FY 2017, to \$13.84 billion. That rate of growth, while about double the rate we now expect in FY 2016, is less than the 4.7% growth we previously expected, and is below the post-recession average rate of increase.

Turning now to the State's second largest revenue, the Sales and Use Tax, we have revised our projections slightly upward for both fiscal years. March and April collections were strong, bringing the year-to-date growth rate to 5.2%, and we believe that rate will persist through the end of the fiscal year. This has led us to bump our FY 2016 estimate up by \$60 million. We still hold to our view that this rate of growth will not carry into FY 2017, but due to the improved outlook for the current year, we now assume 3.8% growth for FY 2017 rather than 3.5%, which is \$93 million above our prior estimate.

The other significant change in revenues concerns the sales and corporation business taxes on energy. Both the Executive and the OLS have revised the estimate for these receipts down by \$118 million in FY 2016 and \$16 million in FY 2017.

Figures 4 and 5 compare the OLS revised estimates to the Executive's revised forecasts for FY 2016 and FY 2017, respectively. There is no significant difference in the two forecasts for the State's three major taxes in FY 2016. Differences are slightly more pronounced for FY 2017. The Executive is assuming net GIT growth of 3.5%, compared to the OLS forecast of a net 3% increase. For the Sales Tax, the Executive is holding to its 3% growth projection, compared to our estimate of a 3.8% increase. The difference in the respective forecasts for the Corporation Business Tax is unchanged from last month. There are minor differences between us in the forecast for a few other taxes that do not much affect the bottom line.

Figure 4

<b>FY 2016 Revenue Estimates</b>			
<i>\$ in Millions</i>			
	<b>Executive Revised May 2016</b>	<b>OLS Revised May 2016</b>	<b>Difference</b>
Gross Income Tax	\$13,408.0	\$13,440.0	\$32.0
Sales Tax	\$9,315.8	\$9,335.0	\$19.2
Corporation Business Tax	\$2,336.0	\$2,280.0	-\$56.0
All Other Revenues	\$8,138.4	\$8,127.9	-\$10.5
<b>Total Budget Revenues</b>	<b>\$33,198.2</b>	<b>\$33,182.9</b>	<b>-\$15.3</b>

\* May 19, 2016. Includes certain amounts from Treasury's revised revenue forecast.

Figure 5

<b>FY 2017 Revenue Estimates</b>			
<i>\$ in Millions</i>			
	<b>Executive Revised May 2016</b>	<b>OLS Revised May 2016</b>	<b>Difference</b>
Gross Income Tax	\$13,982.3	\$13,840.0	-\$142.3
Sales Tax	\$9,597.4	\$9,690.0	\$92.6
Corporation Business Tax	\$2,336.0	\$2,180.0	-\$156.0
<i>CBT Treasury Proposal</i>	<i>\$135.0</i>	<i>\$135.0</i>	<i>\$0.0</i>
All Other Revenues	\$8,541.4	\$8,575.0	\$33.6
<b>Total Budget Revenues</b>	<b>\$34,592.1</b>	<b>\$34,420.0</b>	<b>-\$172.1</b>

\* May 19, 2016. Includes certain amounts from Treasury's revised revenue forecast.

I want to emphasize that the adjustments to our revenue outlook do not stem from a significant change in economic circumstances. Revenues are growing, not declining. The OLS is acknowledging results to date that fell short of our expectations, and is taking a more restrained view of how a slow-growing economy is likely to affect our revenues going forward. Our remarks to you in April referenced revenue forecast error as one of several items of uncertainty present in the Governor's budget plan. But, as we have

commented previously, errors that seem small by one measurement have larger consequences when placed in other contexts.

We observed in the *OLS Tax and Revenue Outlook* in April that the FY 2017 surplus, then at 2.3% of budgeted expenditures was low both by New Jersey historical standards and by national standards. Under the Executive's revised budget plan, surplus is now at 1.8%. The FY 2016 surplus proved insufficient to absorb the impact of a revenue forecast that misses its mark by a degree that is within normal forecasting variability, and various budget solutions were necessary. Risks to the FY 2017 budget remain, and we should be concerned whether this diminished cushion is adequate in light of those risks. And providing a cushion for normal variability is the easier role that a budget surplus should be expected to play. The more difficult role for a surplus is to counteract the onset of truly hard times for budget-makers, those years when worsening economic conditions produce much more significant forecasting variances.

The difficult choices placed before you in February have regrettably become even more challenging. The staff of the Office of Legislative Services remains prepared to provide whatever assistance we can as you continue your arduous task of budget-making.

## Revised Fiscal Year 2016 Revenue Estimates

*Millions of \$*

<u>Revenue Source</u>	<u>Executive Est.</u> <u>February 2016</u>	<u>Executive Est.</u> <u>May 2016</u>	<u>Executive Change</u> <u>Feb to May</u>	<u>OLS Estimate</u> <u>May 2016</u>	<u>Diff. OLS -</u> <u>Executive</u>
<b>Major Taxes:</b>					
<b>Sales Tax, Total</b>	<b>\$8,769.9</b>	<b>\$8,671.6</b>	<b>-\$98.3</b>	<b>\$8,690.8</b>	<b>\$19.2</b>
<i>Sales Tax, Base</i>	9,315.8	9,315.8	\$0.0	9,335.0	19.2
<i>Dedicated Transfer to PTRF</i>	-705.9	-702.8	\$3.1	-702.8	0.0
<i>Sales Tax, Energy</i>	160.0	58.6	-\$101.4	58.6	0.0
<b>Corporation Business Tax, Total</b>	<b>\$2,358.0</b>	<b>\$2,341.5</b>	<b>-\$16.5</b>	<b>\$2,285.5</b>	<b>-\$56.0</b>
<i>Corporation Business Tax, Base</i>	2,336.0	2,336.0	\$0.0	2,280.0	-56.0
<i>Corporation Business Tax, Energy</i>	22.0	5.5	-\$16.5	5.5	0.0
Inheritance Taxes	828.1	828.1	\$0.0	840.0	11.9
Motor Fuels Tax	556.6	549.5	-\$7.0	548.0	-1.5
Insurance Premiums Tax	668.7	668.7	\$0.0	640.0	-28.7
Realty Transfer Fee	309.1	309.1	\$0.0	311.9	2.8
Motor Vehicle Fees	479.1	479.1	\$0.0	479.1	0.0
Cigarette Tax	163.6	170.0	\$6.4	187.8	17.8
Petroleum Products Gross Receipts Tax	218.1	218.1	\$0.0	213.0	-5.1
Corp. Business Tax - Banks and Financial	155.3	145.0	-\$10.3	140.0	-5.0
Alcoholic Beverage Excise Tax	109.5	109.5	\$0.0	107.0	-2.5
Tobacco Products Wholesale Tax	22.4	22.4	\$0.0	22.4	0.0
Public Utilities Excise Tax	15.6	15.6	\$0.0	15.6	0.0
<b>Subtotal, Major Taxes</b>	<b>\$14,653.9</b>	<b>\$14,528.1</b>	<b>-\$125.8</b>	<b>\$14,481.1</b>	<b>-\$47.0</b>
<b>Misc. Taxes, Fees and Revenues</b>					
Assessment on Property Sold Over \$1 Million	114.8	114.8	\$0.0	120.0	5.2
Medicaid Uncomp. Care Reimbursement	453.6	488.2	\$34.6	488.2	0.0
Other	2,380.3	2,216.3	-\$164.0	2,216.2	0.0
<b>Subtotal, Misc. Revenues</b>	<b>\$2,948.6</b>	<b>\$2,819.3</b>	<b>-\$129.3</b>	<b>\$2,824.5</b>	<b>\$5.2</b>
<b>Interfund Transfers</b>					
State Lottery Fund	965.0	965.0	\$0.0	965.0	0.0
Other	500.5	500.7	\$0.2	500.7	0.0
<b>Subtotal, Interfund Transfers</b>	<b>\$1,465.5</b>	<b>\$1,465.7</b>	<b>\$0.2</b>	<b>\$1,465.7</b>	<b>\$0.0</b>
<b>TOTAL GENERAL FUND</b>	<b>\$19,068.0</b>	<b>\$18,813.0</b>	<b>-\$255.0</b>	<b>\$18,771.2</b>	<b>-\$41.8</b>
<b>Property Tax Relief Fund (Income Tax)</b>					
<i>PTRF Transfer from GF (Sales Tax)</i>	<i>\$728.0</i>	<i>\$724.9</i>	<i>-\$3.1</i>	<i>\$724.9</i>	<i>\$0.0</i>
<b>Casino Revenue Fund (CRF)</b>	<b>\$203.2</b>	<b>\$208.7</b>	<b>\$5.5</b>	<b>\$203.2</b>	<b>-\$5.5</b>
CRF Taxes	\$193.6	\$199.1	\$5.5	\$193.6	-\$5.5
CRF Other	\$9.5	\$9.5	\$0.0	\$9.5	\$0.0
<b>Casino Control Fund</b>	<b>\$42.9</b>	<b>\$42.9</b>	<b>\$0.0</b>	<b>\$42.9</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>GRAND TOTAL, ALL FUNDS</b>	<b>\$33,800.8</b>	<b>\$33,198.2</b>	<b>-\$602.6</b>	<b>\$33,182.9</b>	<b>-\$15.3</b>

May 18, 2016. Includes Treasury's revised revenue forecast.  
OLS adjusted misc. revenues per Treasurer's revised forecast.



## Revised Fiscal Year 2017 Revenue Estimates

Millions of \$

Revenue Source	<u>Executive Est.</u> February 2016	<u>Executive Est.</u> May 2016	<u>Executive Change</u> Feb to May	<u>OLS Estimate</u> May 2016	<u>Diff: OLS -</u> <u>Executive</u>
<b>Major Taxes:</b>					
<b>Sales Tax, Total</b>	<b>\$9,050.3</b>	<b>\$9,032.6</b>	<b>-\$17.7</b>	<b>\$9,125.2</b>	<b>\$92.6</b>
<i>Sales Tax, Base</i>	9,597.4	9,597.4	\$0.0	9,690.0	92.6
<i>Dedicated Transfer to PTRF</i>	-727.4	-729.0	-\$1.6	-729.0	0.0
<i>Sales Tax, Energy</i>	180.3	164.2	-\$16.1	164.2	0.0
<b>Corporation Business Tax, Total</b>	<b>\$2,358.0</b>	<b>\$2,493.0</b>	<b>\$135.0</b>	<b>\$2,337.0</b>	<b>-\$156.0</b>
<i>Corporation Business Tax, Base</i>	2,336.0	2,471.0	\$135.0	2,315.0	-156.0
<i>Corporation Business Tax, Energy</i>	22.0	22.0	\$0.0	22.0	0.0
Inheritance Taxes	848.5	848.5	\$0.0	880.0	31.5
Motor Fuels Tax	545.6	540.0	-\$5.5	560.0	20.0
Insurance Premiums Tax	688.7	688.7	\$0.0	660.0	-28.7
Realty Transfer Fee	330.4	330.4	\$0.0	338.4	8.0
Motor Vehicle Fees	515.6	515.6	\$0.0	515.6	0.0
Cigarette Tax	126.5	149.0	\$22.5	170.4	21.4
Petroleum Products Gross Receipts Tax	218.1	218.1	\$0.0	217.0	-1.1
Corp. Business Tax - Banks and Financial	155.3	150.0	-\$5.3	140.0	-10.0
Alcoholic Beverage Excise Tax	110.8	110.8	\$0.0	109.0	-1.8
Tobacco Products Wholesale Tax	22.4	22.4	\$0.0	22.4	0.0
Public Utilities Excise Tax	15.6	15.6	\$0.0	15.6	0.0
<b>Subtotal, Major Taxes</b>	<b>\$14,985.7</b>	<b>\$15,114.6</b>	<b>\$128.9</b>	<b>\$15,090.6</b>	<b>-\$24.1</b>
<b>Misc. Taxes, Fees and Revenues</b>					
Assessment on Property Sold Over \$1 Million	124.5	124.5	\$0.0	129.0	4.5
Medicaid Uncomp. Care Reimbursement	386.8	371.9	-\$14.9	371.9	0.0
Other	2,456.1	2,534.0	\$77.9	2,534.0	0.0
<b>Subtotal, Misc. Revenues</b>	<b>\$2,967.4</b>	<b>\$3,030.4</b>	<b>\$63.0</b>	<b>\$3,034.9</b>	<b>\$4.5</b>
<b>Interfund Transfers</b>					
State Lottery Fund	965.0	965.0	\$0.0	965.0	0.0
Other	489.1	489.2	\$0.1	489.2	0.0
<b>Subtotal, Interfund Transfers</b>	<b>\$1,454.1</b>	<b>\$1,454.2</b>	<b>\$0.1</b>	<b>\$1,454.2</b>	<b>\$0.0</b>
<b>TOTAL GENERAL FUND</b>	<b>\$19,407.2</b>	<b>\$19,599.2</b>	<b>\$192.0</b>	<b>\$19,579.6</b>	<b>-\$19.6</b>
<b>Property Tax Relief Fund (Income Tax)</b>					
<i>PTRF Transfer from GF (Sales Tax)</i>	<b>\$749.5</b>	<b>\$751.1</b>	<b>\$1.6</b>	<b>\$749.5</b>	<b>-\$1.6</b>
<b>Casino Revenue Fund (CRF)</b>					
CRF Taxes	\$190.2	\$198.8	\$8.6	\$190.2	-8.6
CRF Other	\$9.8	\$9.8	\$0.0	\$9.8	0.0
<b>Casino Control Fund</b>	<b>\$50.3</b>	<b>\$50.3</b>	<b>\$0.0</b>	<b>\$50.3</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>GRAND TOTAL, ALL FUNDS</b>	<b>\$34,832.2</b>	<b>\$34,592.1</b>	<b>-\$240.2</b>	<b>\$34,420.0</b>	<b>-\$172.1</b>

May 18, 2016. Includes Treasury's revised revenue forecast.

OLS adjusted misc. revenues per Treasurer's revised forecast.

Treasury's corporation business tax revision assumes \$135 million for a delayed BEIP grant conversion, pending Legislative action. For purposes of this display, the OLS revised estimate also incorporates this assumption.