

TESTIMONY PREPARED FOR PRESENTATION TO THE
ASSEMBLY BUDGET COMMITTEE
CATHERINE Z. BRENNAN
OFFICE OF LEGISLATIVE SERVICES
MAY 17, 2017

Good morning Mr. Chairman and Members of the Committee.

With important April tax collections now realized, we are here this morning to provide you with an update of the OLS revenue forecasts for the current and next fiscal years. As you may recall, when we appeared before the committee approximately six weeks ago, we reported that revenues for FY 2017 were performing below their certified targets, and that New Jersey's revenue performance appeared to be echoing national trends, with the majority of states experiencing a softening of state tax collections. Nothing has changed. Like many other states around the country, including California, Massachusetts, Connecticut and Pennsylvania, New Jersey experienced a lackluster April tax filing season.

The detail we are providing the committee this morning reflects a comparison of the OLS' revised forecast relative to the Executive's update which revised FY 2017 revenues downward by \$526.9 million, but increased FY 2018 collections by \$191.0 million. While our forecasts of the major taxes were largely set yesterday morning prior to our appearance before the Senate Budget and Appropriations Committee, we have subsequently accepted numerous adjustments the State Treasurer announced with regard to the miscellaneous non-tax revenues which comprise the balance of Anticipated Revenues (Schedule 1). We have also accepted the Executive's motor fuels tax and petroleum products gross receipts tax revenues and have included the Executive's newly announced tax administration plan projected to yield approximately \$200.0 million in FY 2018. However, while the Executive's display incorporates this revenue enhancement into its FY 2018 sales and use tax revenue line, the OLS display separately states this revenue.

Six weeks ago, we informed you that, in the aggregate, OLS revenue forecasts over the two fiscal years combined – FY 2017 and FY 2018 -- were \$436.2 million below the Executive's forecast, a difference of 0.6% (six-tenths of one percent). This morning, relative to the Administration's downward revisions, the OLS aggregate forecasts are now just \$115.5 million below the Executive over the two fiscal years. Specifically, for the current fiscal year, the OLS forecast now stands \$115.2 million above Treasury's estimate, while in the out year, our projection now falls \$230.7 million below the Executive's forecast.

While most of the major taxes are performing close to expectations, with a few bright spots I will address shortly, both the **corporation business tax (CBT)** and the **gross income tax (GIT)** are performing weaker than expected, with the CBT accounting for most of the current forecasting revision.

CBT collections through the first ten months of the fiscal year are running 15.4% below last year, compared to the 13% decline we reported six weeks ago. The CBT's year-to-date decline is largely attributable to the accelerated transfer of out-of-state partnership receipts from the CBT to the GIT, which for the first time this year is being done on a monthly basis, rather than as a singular, post-fiscal year adjustment and is impacting the nominal growth rates of both taxes. Accounting for this factor, underlying CBT growth is up 4.8% in the current year. However, while positive, the CBT would need to grow at an improbable 24.1% through the end of the year to achieve the certified target of 7.6%. Given the current trend, the Executive and the OLS now agree that this target is unlikely to be realized with the Executive forecasting \$2.20 billion for FY 2017 and the OLS \$2.27 billion, with roughly similar forecasts in the out year. The magnitude of the accelerated shift in non-resident partnership income from the CBT to the GIT is the most significant factor depressing CBT growth this year, while underlying CBT growth is also underperforming relative to the GBM expectations.

Let's turn now to the GIT. As mentioned at the outset of these remarks, April collections trailed expectations. While April net income tax collections were up \$266 million, or 12.8%, over last year, April cash receipts were enhanced by the transfer of \$117.0 million in out-of-state partnership withholding receipts from the CBT, and a \$144.0 million drop in refund payments due, in part, to a \$95.1 million increase in TANF monies applied to offset the cost of the enhanced Earned Income Tax Credit (EITC) program. Thus, absent these two factors, April collections were up only \$5.0 million, essentially flat with last year.

Overall, the components which comprise total GIT collections are demonstrating mixed results after ten months. On the positive side, underlying withholding receipts (the largest component of the GIT) are up 3.6%, while refund payments, which are lower than last year, are boosting net revenues. On the other side of the ledger, estimated payments are down 3.3%, while final payments demonstrated essentially zero growth, well below expectations. All these factors considered, the OLS's revised GIT estimate is now just \$6.7 million higher than the Executive's downwardly revised estimate this fiscal year, essentially identical. Weak April estimated and final payments were largely offset by the sizeable year-to-date transfer of \$397.1 million from the CBT to the GIT from out-of-state partnership receipts.

Given the weak April results for estimated and final payments, notwithstanding the strong stock market performance at the end of last year, the OLS continues to hold to its working hypothesis that taxpayer behavior at the end of calendar year 2016 may have been influenced by the anticipation of federal tax rate cuts, causing taxpayers to both delay taking gains and perhaps accelerate deductions at the end of last year. And while the outlook for federal tax reform remains uncertain at this time, the OLS is still anticipating higher growth for next April's payments under the GIT in FY 2018. The OLS estimate for the GIT next fiscal year is a relatively modest \$62.2 million below the Executive's downwardly revised projection.

The state's second largest revenue source, the **sales tax**, is performing in line with OLS expectations. Thus, our estimates for the sales tax are unchanged from six weeks ago as we finalize the fourth month of collections impacted by the recent tax rate reduction. The OLS estimate for the sales tax remains \$55.0 million above the Executive for FY 2017 as the Executive has not revised its FY 2017 projection for this tax. However, the OLS sales tax estimate which was previously \$65.7 million below the Executive for FY 2018 relative to the Governor's Budget Message, now stands \$124.9 million below the Executive's revised forecast

even after excluding the \$200.0 million in new revenue the Executive is anticipating from various tax administration initiatives. Adjusting the Executive's FY 2018 sales tax estimate for the \$200 million revenue enhancement and our calculation of the value of the sales tax rate change under P.L.2016, c.57 suggests the Executive has assumed an underlying sales tax growth rate of approximately 5.4% in the out year, compared to our underlying estimate of 3.5%. Thus, the sales tax now represents the largest source of difference between the Executive and OLS estimates.

Let's turn now to some of the bright spots:

While significantly smaller than the overall CBT, the **corporate tax on banks and financial institutions**, the bulk of which derives from the banking sector, is currently experiencing positive year to date growth of approximately 6.7%. Thus, the OLS is now accepting the Executive's projections as contained within the GBM, while by comparison, the Treasury has increased its estimate above the GBM, by \$14.6 million this year and \$15.7 million next fiscal year.

In addition, the **realty transfer fee (RTF)** and the **cigarette tax** are performing above expectations, and we have adjusted our estimates for these taxes upward accordingly.

Based on growth trends experienced through the end of February, the OLS previously anticipated the realty transfer fee to reach \$342.4 million in FY 2017, which included \$39.8 million in collections in September, the largest monthly amount realized in over a decade. However, robust growth in both March and April increased the year-to-date growth rate of the RTF from 9.4% to approximately 12%. Absent September collections, the current year-to-date growth rate for the realty transfer fee is approximately 9.5%, which the OLS expects to continue for the remaining months of the current fiscal year. Thus, the OLS is projecting approximately \$350.0 million for FY 2017 RTF collections, an 11.7% increase year-over-year, and \$10.5 million above prior expectations. Moreover, the OLS' FY 2018 projection anticipates continued growth, and we are maintaining our previously forecasted growth rate of 7.5% for the out year. The Executive's revised estimates are very similar.

Finally, in recent years, cigarette tax collections have declined by about 2.5% to 3.0% annually. This fiscal year, however, cigarette tax collections are running roughly 0.24% (one-quarter of one percent) above FY 2016, marking the first time in five years that collections have grown through the end of April, perhaps influenced by the cigarette tax rate increase in Pennsylvania which took effect August 1, 2016. Thus, incorporating current year growth, and an enhancement from a lower off-budget debt service payment (for cigarette tax revenue securitization bonds equal to \$3.4 million), the OLS projects on-budget cigarette tax collections to reach \$185.0 million in FY 2017, up \$8.4 million over our estimate six weeks ago. For FY 2018, the OLS is projecting collections of \$181.3 million in on-budget cigarette tax collections, reflecting a return to a more normal 1.5% decline in cigarette tax collections partially offset by a \$6.6 million reduction in the off-budget debt service payment (for cigarette tax revenue securitization bonds). Taken together, over the two fiscal years, the OLS estimates are \$28.4 million above the Executive's revised estimates.

Again, the full side-by-side comparison tables you have been provided display the Treasurer's revised revenues and the OLS revised revenues for FY 2017 and FY 2018. The combined

revenue forecasting difference of \$115.5 million we have presented to you this morning is relatively small by historical standards, a mere 0.2% (two-tenths of one percent) below the Executive's two-year total.

And now, we will do our best to answer any questions you might have.

FOR FURTHER INFORMATION ABOUT THE OLS REVENUE ESTIMATES, PLEASE CONTACT:	
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Revised Fiscal Year 2017 Revenue Estimates

Millions of \$

<u>Revenue Source</u>	<u>Executive Est.</u> <u>February 2017</u>	<u>Executive Est.</u> <u>May 2017</u>	<u>Executive</u> <u>Change Feb to</u> <u>May</u>	<u>OLS Estimate</u> <u>May 2017</u>	<u>Diff: OLS -</u> <u>Executive</u>
Major Taxes:					
Sales Tax, Total	\$8,723.5	\$8,708.3	-\$15.1	\$8,763.7	\$55.3
<i>Sales Tax, Base</i>	9,294.7	9,294.7	\$0.0	9,350.0	55.3
<i>Dedicated Transfer to PTRF</i>	-719.0	-718.0	\$1.0	-718.0	0.0
<i>Sales Tax, Energy</i>	147.8	131.7	-\$16.1	131.7	0.0
Corporation Business Tax, Total	\$2,481.0	\$2,205.4	-\$275.6	\$2,267.0	\$61.6
<i>Corporation Business Tax, Base</i>	2,471.0	2,203.4	-\$267.6	2,265.0	61.6
<i>Corporation Business Tax, Energy</i>	10.0	2.0	-\$8.0	2.0	0.0
Inheritance Taxes	703.9	752.4	\$48.5	722.0	-30.4
Motor Fuels Tax	562.0	541.7	-\$20.3	541.7	0.0
Insurance Premiums Tax	615.5	530.5	-\$85.0	550.0	19.5
Realty Transfer Fee	339.3	351.2	\$11.9	350.0	-1.2
Motor Vehicle Fees	514.2	514.2	\$0.0	514.2	0.0
Cigarette Tax	176.6	170.7	-\$6.0	185.0	14.3
Petroleum Products Gross Receipts Tax	939.0	877.7	-\$61.3	877.7	0.0
<i>Less: Petroleum Products GR Capital Reserves</i>	-416.2	-334.6	\$81.7	-334.6	0.0
Corp. Business Tax - Banks and Financial	172.7	187.3	\$14.6	172.7	-14.6
Alcoholic Beverage Excise Tax	110.3	105.4	-\$4.9	106.0	0.6
Tobacco Products Wholesale Tax	23.8	23.4	-\$0.4	23.8	0.4
Public Utilities Excise Tax	17.8	17.8	\$0.0	17.8	0.0
Subtotal, Major Taxes	\$14,963.3	\$14,651.4	-\$311.9	\$14,757.0	\$105.6
Misc. Taxes, Fees and Revenues					
Medicaid Uncomp. Care Reimbursement	357.8	362.3	\$4.6	362.3	0.0
Settlements	140.0	26.0	-\$114.0	26.0	0.0
Federal Funds - Graduate Medical Education	123.3	123.3	\$0.0	123.3	0.0
Public Utility Taxes (State Retention)	129.0	129.0	\$0.0	129.0	0.0
Assessment on Property Sold Over \$1 Million	137.8	137.8	\$0.0	145.6	7.8
Telephone Assessment	121.3	124.0	\$2.7	124.0	0.0
Hotel Occupancy Tax	102.3	102.3	\$0.0	102.3	0.0
Asset Sales	0.0	0.0	\$0.0	0.0	0.0
Fringe Benefit Recoveries (Interdepartmental)	697.9	699.1	\$1.2	699.1	0.0
Interdepartmental Accounts, Other	100.4	101.2	\$0.8	101.2	0.0
Other	1,078.8	1,070.1	-\$8.7	1,070.1	0.0
Subtotal, Misc. Revenues	\$2,988.6	\$2,875.2	-\$113.4	\$2,883.0	\$7.8
Interfund Transfers					
State Lottery Fund	970.0	970.0	\$0.0	970.0	0.0
Unclaimed Personal Property Trust Fund	172.0	172.0	\$0.0	172.0	0.0
State Disability Benefit Fund	38.9	38.9	\$0.0	38.9	0.0
Enterprise Zone Assistance Fund	71.1	70.9	-\$0.2	70.9	0.0
Other	202.6	202.7	\$0.1	202.7	0.0
Subtotal, Interfund Transfers	\$1,454.6	\$1,454.4	-\$0.1	\$1,454.4	\$0.0
TOTAL GENERAL FUND	\$19,406.5	\$18,981.1	-\$425.5	\$19,094.4	\$113.4
Property Tax Relief Fund (Income Tax)					
<i>PTRF Transfer from GF (Sales Tax)</i>	<i>\$741.1</i>	<i>\$740.3</i>	<i>-\$0.8</i>	<i>\$740.3</i>	<i>\$0.0</i>
Casino Revenue Fund (CRF)	\$216.1	\$217.4	\$1.3	\$212.5	-\$4.9
CRF Taxes	\$208.6	\$209.9	\$1.2	\$205.0	-\$4.9
CRF Other	\$7.5	\$7.5	\$0.1	\$7.5	\$0.0
Casino Control Fund	\$49.6	\$49.6	\$0.0	\$49.6	\$0.0
Gubernatorial Elections Fund	\$0.7	\$0.7	\$0.0	\$0.7	\$0.0
GRAND TOTAL, ALL FUNDS	\$34,354.3	\$33,827.4	-\$526.9	\$33,942.6	\$115.2

May 16, 2017. Subsequent to Treasury's revised revenue forecast. OLS figures adjusted for revenues with no analytical difference. The OLS accepts the Executive's motor fuels and petroleum products gross receipts estimates.

Revised Fiscal Year 2018 Revenue Estimates

Millions of \$

<u>Revenue Source</u>	<u>Executive Est.</u> <u>February 2017</u>	<u>Executive Est.</u> <u>May 2017</u>	<u>Executive</u> <u>Change Feb to</u> <u>May</u>	<u>OLS Estimate</u> <u>May 2017</u>	<u>Diff: OLS -</u> <u>Executive</u>
Major Taxes:					
Sales Tax, Total	\$8,870.7	\$8,871.8	\$1.1	\$8,747.0	-\$124.9
Sales Tax, Base	9,450.7	9,509.9	\$59.1	9,385.0	-124.9
Dedicated Transfer to PTRF	-745.0	-761.0	-\$16.0	-761.0	0.0
Sales Tax, Energy	165.0	123.0	-\$42.0	123.0	0.0
Corporation Business Tax, Total	\$2,606.5	\$2,377.8	-\$228.7	\$2,362.4	-\$15.4
Corporation Business Tax, Base	2,594.5	2,375.4	-\$219.1	2,360.0	-15.4
Corporation Business Tax, Energy	12.0	2.4	-\$9.6	2.4	0.0
Executive Tax Initiatives*	0.0	200.0	\$200.0	200.0	0.0
Inheritance Taxes	657.5	745.8	\$88.2	731.0	-14.8
Motor Fuels Tax	573.3	552.5	-\$20.7	552.5	0.0
Insurance Premiums Tax	661.6	570.3	-\$91.3	577.5	7.2
Realty Transfer Fee	369.8	382.8	\$13.0	376.3	-6.5
Motor Vehicle Fees	498.2	513.2	\$15.0	498.2	-15.0
Cigarette Tax	173.0	167.2	-\$5.8	181.3	14.1
Petroleum Products Gross Receipts Tax	1,457.9	1,487.2	\$29.3	1,487.2	0.0
Less: Petroleum Products GR Capital Reserves	-926.5	-940.2	-\$13.6	-940.2	0.0
Corp. Business Tax - Banks and Financial	185.7	201.4	\$15.7	185.7	-15.7
Alcoholic Beverage Excise Tax	111.9	107.0	-\$4.9	108.0	1.0
Tobacco Products Wholesale Tax	24.9	24.5	-\$0.4	24.9	0.4
Public Utilities Excise Tax	18.4	18.4	\$0.0	18.4	0.0
Subtotal, Major Taxes	\$15,283.0	\$15,279.65	-\$3.3	\$15,110.20	-\$169.4
Misc. Taxes, Fees and Revenues					
Medicaid Uncomp. Care Reimbursement	337.6	334.2	-\$3.4	334.2	0.0
Settlements	75.0	300.0	\$225.0	300.0	0.0
Federal Funds - Graduate Medical Education	141.0	141.0	\$0.0	141.0	0.0
Public Utility Taxes (State Retention)	133.0	133.0	\$0.0	133.0	0.0
Assessment on Property Sold Over \$1 Million	144.6	144.6	\$0.0	153.0	8.4
Telephone Assessment	134.3	137.0	\$2.7	137.0	0.0
Hotel Occupancy Tax	106.4	106.4	\$0.0	106.4	0.0
Asset Sales	325.0	340.0	\$15.0	340.0	0.0
Fringe Benefit Recoveries (Interdepartmental)	689.5	669.0	-\$20.5	669.0	0.0
Interdepartmental Accounts, Other	95.8	96.0	\$0.3	96.0	0.0
Other	1,160.9	1,161.3	\$0.4	1,161.3	0.0
Subtotal, Misc. Revenues	\$3,343.1	\$3,562.7	\$219.5	\$3,571.1	\$8.4
Interfund Transfers					
State Lottery Fund	1,014.0	1,014.0	\$0.0	1,014.0	0.0
Unclaimed Personal Property Trust Fund	160.0	170.0	\$10.0	170.0	0.0
State Disability Benefit Fund	38.5	38.5	\$0.0	38.5	0.0
Enterprise Zone Assistance Fund	66.7	66.0	-\$0.8	66.0	0.0
Other	213.2	213.4	\$0.2	213.4	0.0
Subtotal, Interfund Transfers	\$1,492.4	\$1,501.9	\$9.5	\$1,501.9	\$0.0
TOTAL GENERAL FUND	\$20,118.5	\$20,344.2	\$225.6	\$20,183.1	-\$161.0
Property Tax Relief Fund (Income Tax)					
PTRF Transfer from GF (Sales Tax)	\$14,435.0	\$14,382.2	-\$52.8	\$14,320.0	-\$62.2
Casino Revenue Fund (CRF)	\$767.1	\$783.9	\$16.8	\$783.9	\$0.0
CRF Taxes	\$223.6	\$225.0	\$1.4	\$217.5	-\$7.5
CRF Other	\$216.2	\$217.5	\$1.3	\$210.0	-7.5
Casino Control Fund	\$7.4	\$7.5	\$0.1	\$7.5	0.0
Gubernatorial Elections Fund	\$50.0	\$50.0	\$0.0	\$50.0	\$0.0
GRAND TOTAL, ALL FUNDS	\$0.7	\$0.7	\$0.0	\$0.7	\$0.0
GRAND TOTAL, ALL FUNDS	\$35,595.0	\$35,786.0	\$191.0	\$35,555.3	-\$230.7

May 16, 2017. Subsequent to Treasury's revised revenue forecast. OLS figures adjusted for revenues with no analytical difference.

The OLS accepts the Executive's motor fuels and petroleum products gross receipts estimates.

* The Executive's tax initiatives proposal is valued at approximately \$200.0 million. OLS displays this separately from the sales tax.