



**Understanding New Jersey's Revenue Outlook
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NOW THAT MCREEVEY HAS BEEN TOLD HE HAS MORE MONEY THAN HE THOUGHT IN FEBRUARY WILL HE REDUCE HIS TAX INCREASES BY CORRESPONDING AMOUNTS?

Tomorrow, Treasurer McCormac will release the revised Fiscal Year 2004 budgets and update the administration's 2005 budget target. Americans for Tax Reform (ATR) is forecasting revenues will be \$800 million to \$1 billion higher in FY 2004 than the administration forecasted for this time last year. The Treasurer will be probably use a number around \$500 million tomorrow, but that is a reflection of the changes from just February – meaning the forecast for the current year has been revised up \$500 million in less than 4 months. In February they revised their previous estimate more than \$380 million. We could be talking about the state taking in \$1 billion MORE THAN EXPECTED.

The budget had already assumed significant growth of \$700 million, so the new revenue is actually \$800 million to \$1 billion on top of the \$700 million increase already accounted for. Tomorrow you will also hear that revenues will “dip” in the next fiscal year – this is complete hodgepodge revenues will be accelerating faster than they did in the late 1990's although it may be a percent slower than the enormous growth about to reported tomorrow.

This is the result of the Bush Tax Cuts placing an astonishing \$9.5 billion of tax dollars back into the New Jersey economy in Calendar Year 2003 and \$10 billion in Calendar Year 2004. ATR is forecasting another \$11.5 billion to be returned in 2005 as well.

The importance of this cannot be understated and has real implications for the \$2.1 billion of tax increases being proposed by the McGreevey administration for next fiscal year. The previous year budget battle is instructive of how McGreevey will proceed.

Last year, McGreevey reported to legislature that he needed to raise taxes \$630 million to fund the government in fiscal year 2004. Upon finding out however, that George Bush was bailing him put with \$561 million, revenues were undercounted by \$630 million in the current fiscal year, and the Bush tax cut was going to increase growth and hence

revenues another \$600 million McGreevey never reduced his tax increase. At the end of the day he got \$600 million of tax increases, \$561 million from the federal government, \$630 million of undercounted revenues, and now \$900 million from the growth effects of the Bush tax cut. And this is man that continues to cry poverty.

Star-Ledger reporter Joe Donohue went to the Treasurer and specifically asked the Treasurer if the Bush tax cuts would spur new tax revenues. The paper reported “But Treasurer John McCormac said he doubts the Bush tax cuts will have a major impact in the upcoming budget year.” 6/15/03. McCormac has no credibility tomorrow when he seeks to take claim for the revenue growth. His staff is either incompetent to recognize that this was going to happen or they purposely low balled to increase taxes. That is why ATR expects him to again lowball next year’s growth number – to push the McGreevey \$2.1 billion of tax increases.

Background

Gross Domestic Product (GDP) the widely accepted measure of economic growth has accelerated far above the normal rate of growth since the tax cut was put into place, which is boosting revenues at the federal and state levels way above what was expected by government forecasters. The non partisan Congressional Budget Office (CBO) last week claimed the have underestimated revenue by as much as \$30 to \$40 billion and the deficit may be reduced by as much as \$100 billion by the end of the federal fiscal year. This will also have a significant effect on NJ's revenues.

GDP's long run historical average is 3.2 percent, yet since the tax cut went into the effect, GDP has averaged 5.5 percent on a quarterly average. This is fastest three quarters of growth since 1984 (ironically the last time federal taxes were substantially cut). GDP and personal income (which is soaring) are the drivers for tax revenues.

Even assuming NJ grew in proportion with the national average, the tax cuts have added an astonishing 2.5 percent to the state’s growth rate. In CY 2003 ATR estimates \$9.5 billion was returned to NJ residents with an additional \$10 billion being returned in CY 2004. All of this is taxable by the state when used within the state’s economy. (Dwarfing mcgreevey tax increases). The average taxpayer saved roughly \$2,500.

ATR has long made the argument that cutting federal taxes disproportionately benefits NJ over other states. Since NJ taxes are collected in Washington and re-sent to other states, the federal tax system removes a net \$26 billion per year from the state's economy. Federal tax cuts have a reverse effect by increasing the net amount of cash left into the state.

ATR is calling for another monster year in fy 2005 since half of the \$10 billion from CY 2004 will still be saved, the tax cuts expiring will be extended and further Alternative

Minimum Tax protections will also be approved. As such ATR expects \$11.5 billion of savings in CY 05 with half of that available in the state's FY 05 budget.

All told, the lower rates put into place by Bush has elevated the tax revenue baseline for state tax collections in the future.

Federal Tax Previous History with NJ revenues

Two only two major federal tax cuts since 1980 prove this theory to be correct and is what is driving state revenues so much. I might add for this and next year contrary to what the Treasury Dept is saying about a slowdown.

The significant rate reductions under Reagan led NJ to become an economic powerhouse throughout the 80's. The state outpaced the nation in economic growth, personal income, and employment. In fact, state economic growth outpaced federal growth by more than 30 percent from 1981-1985. However, this trend reversed following the subsequent federal tax increases.

This trend reversed again when Clinton signed into law a federal capital gains tax reduction from 28 to 20 percent in 1997. The capital gains cut at the federal level contributed to the largest collection of state income tax revenues for any three-year period since the state enacted the income tax.

The increase of revenue doubled the amount of revenue generated from the Florio tax increases. For the period of fiscal year 1998-2000, state revenues increased nearly \$2.1 Billion (inflation-adjusted dollars) despite numerous tax cuts. The next largest increase was FY91-93, in which revenues grew at half the rate as the 98-00 period despite Florio doubling the income tax rates. All told, federal tax policy has an enormous impact on NJ economic growth.

The 2003 tax cut was a combination of both the 1981 Reagan rate cuts and the 1997 capital gains tax reduction. So not only has growth increased, the capital gains and dividend tax cuts boosted shareholder wealth \$2.5 trillion. This is also boosting capital gains tax revenue in addition to the revenue from the increased economic growth.

Below is an excerpt from the Star Ledger article dated June 15, 2003

Republicans also say President Bush's recent income tax cuts will provide more tax revenue for New Jersey. They say wealthy New Jerseyans will take the money they save from federal income taxes and boost the economy by spending more and investing in ventures that would create jobs.

A recent analysis by Daniel Clifton of the Americans for Tax Reform, a conservative group, agrees with this theory, noting that New Jersey residents have among the highest incomes in the nation.

"The tax plan is directly targeted at New Jersey's economy, more than any other state, and thus will provide an enormous boom to state revenues in 2004," according to the analysis.

But Treasurer John McCormac said he doubts the Bush tax cuts will have a major impact in the upcoming budget year.

McCormac was dead wrong on this and the April numbers which will be far better than estimated is the proof