ANALYSIS OF THE NEW JERSEY

FISCAL YEAR 2005 - 2006 BUDGET

TAX AND REVENUE OUTLOOK

PREPARED BY

OFFICE OF LEGISLATIVE SERVICES

NEW JERSEY LEGISLATURE

MARCH 2005

NEW JERSEY STATE LEGISLATURE

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THE FY 2005 AND FY 2006 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 2006 appropriations act. The OLS revenue estimates reflect a careful review of current State revenue collections, revisions to statutory law, historic revenue collection patterns, and a variety of economic data and forecasts.

The OLS projects that FY 2005 and FY 2006 revenues will be $287 million greater than the estimates in the FY 2006 Governor's Budget Recommendation. Specifically:

- For FY 2005, the OLS revenue estimates are $87 million above the Executive budget estimates (page 4).
- For FY 2006, the OLS revenue estimates are $200 million above the Executive budget estimates (page 5).

The FY 2006 Budget Recommendation assumes $1.26 billion in new revenues that will require legislation (pages 11 and 12). For analytical comparison purposes, the OLS assumes these new revenues will be fully realized. However, such realization will depend on actions taken by the Legislature and the Executive and subsequent implementation.

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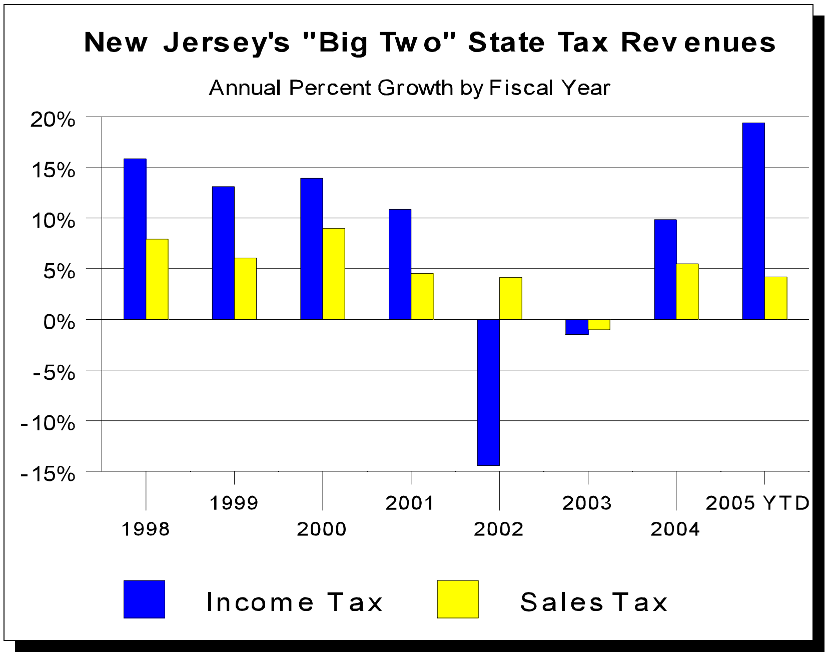


State tax revenue collections depend heavily on the gross income tax and the sales tax. These two revenues typically account for about 60% of budgeted revenues each year. After an extraordinarily difficult two-year period in FY 2002 and FY 2003, these "Big Two" revenues have rebounded. The recent growth patterns are shown in Figure 1:

- Income tax collections plummeted by an unprecedented 14.4% in FY 2002 and fell another 1.5% in FY 2003. But FY 2004 revenues grew by 10%, and through the end of February, FY 2005 collections are up 19.4% year-to-date. A significant source of this year's growth is the tax rate increase on high-income taxpayers.

- Sales tax collections are growing at rates close to the long run historical average of just over 5%. In FY 2004, the sales tax grew by 5.5%, and through the end of February, FY 2005 collections are up 4.2% year-to-date.

Figure 2 contains a more detailed display of current FY 2005 revenue collections through the end of February. Other key points include:

- Corporation business tax (CBT) proceeds have been running below prior year levels since the second payment of Tax Year 2004. Current year-to-date collections are 5.1% below last year. CBT banks and financial institutions revenues are down 57.8%.

- Realty transfer fee revenues are up 73.5% so far this fiscal year, a second year of strong growth, spurred by strong home sales fueled in part by low interest rates, and a series of fee increases.

Recap: FY 2005 Collections to Date

Figure 2
FY 2005 Year-To-Date
Selected Revenue Comparison
Through the End of February 2005 vs. February 2004

($ millions)

Revenue Source	FY 2004 Actual Year-To-Date	FY 2005 Actual Year-To-Date	FY 2005 Actual Year-To-Date % Change	FY 2005 Year-End Treasury % Change Target
Gross Income Tax	$4,245.5	$5,071.2	19.4%	22.4%
Sales Tax *	3,638.0	3,789.2	4.2%	4.1%
Corporation Business Tax	1,053.6	999.9	(5.1)%	(8.3)%
Lottery	503.1	514.0	2.2%	0.6%
Motor Fuels *	323.2	312.5	(3.3)%	(0.3)%
Motor Vehicle Fees	73.4	104.1	41.9%	15.6%
*MV Fees (Total) ** *	*273.0*	*300.5*	*10.1%*	*9.0%*
Casino	292.0	300.4	2.9%	3.8%
Inheritance Taxes	363.7	336.8	(7.4)%	(3.1)%
Insurance Premiums	116.5	129.5	11.1%	3.4%
Cigarette (Budgeted)	351.4	374.7	6.7%	3.9%
*Cigarette (Total)****	*501.4*	*524.7*	4.7%	*3.1%*
Petroleum Products *	121.7	154.3	26.8%	15.6%
Alcohol Excise *	46.5	47.1	1.1%	(0.4)%
CBT -- Banks & Financials	57.4	24.2	(57.8)%	(39.9)%
Realty Transfer Fee *	124.0	215.1	73.5%	51.9%

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 2005 contained in the proposed FY 2006 budget.
** Revenues represent seven months of cash collections. All others represent eight months of cash collections.*
*** Motor Vehicle Fees (Total) includes the off-budget dedication of $199.6 million in FY 2004 and $196.4 million in FY 2005 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 2004 and FY 2005.*

Fiscal Year 2005 Revenue Estimates

Figure 3
Fiscal Year 2005 Revenue Estimates
($ millions)

	Approp. Act (7/1/04)	Executive Revised		OLS	
		Amount (Feb.)	$ Change From Approp.	Amount (March)	OLS vs. Exec.
Gross Income Tax	$8,855	$9,055	$200	$9,100	$45
Sales Tax	6,600	6,520	(80)	6,520	0
Corporation Business Tax	2,500	2,162	(338)	2,162	0
Realty Transfer Fee	286	345	59	390	45
Revenue Securitizations	1,930	1,930	0	1,930	0
Other Revenues	7,430	7,285	(145)	7,282	(3)
Grand Total, All Funds	$27,601	$27,297	($304)	$27,384	$87

See Appendix for additional detail. Numbers may not add due to rounding.

Figure 3 presents the FY 2005 revenue certification from the Appropriations Act (July 2004), 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 2005 Executive:

- In February, the Executive revised estimates for all revenues downward by a net $304 million from the level certified in the FY 2005 Appropriations Act.
- The estimate for the income tax is up $200 million.
- The estimate for the sales tax is down $80 million.
- The estimate for the corporation business tax is down $338 million.
- The estimate for the realty transfer fee is up $59 million.

FY 2005 Office of Legislative Services:

- The OLS's total revenue estimate for FY 2004 is **$87 million above** the Executive's revised projection.
- The OLS estimate for the income tax is $45 million higher than the Executive.
- The OLS estimate for the sales tax is the same as the Executive.
- The OLS estimate for the corporation business tax is the same as the Executive.
- The OLS estimate for the realty transfer fee is $45 million higher than the Executive.

Fiscal Year 2006 Revenue Estimates

Figure 4
Fiscal Year 2006 Revenue Estimates
($ millions)

	Executive		OLS		Difference OLS vs. Exec.
	Amount	Change	Amount	Change	
Gross Income Tax*	$9,520	5.1%	$9,660	6.2%	$140
Sales Tax*	6,850	5.1%	6,850	5.1%	0
Corporation Business Tax	2,155	(0.3)%	2,155	(0.3)%	0
Realty Transfer Fee	405	17.4%	455	16.7%	50
Tax Changes*	1,260	--	1,260	--	0
Other Revenues	7,223	(0.1)%	7,233	(0.1)%	10
Grand Total, All Funds	$27,413	0.4%	$27,613	0.8%	$200

See Appendix for additional detail. Numbers may not add due to rounding. "Change" is from FY 2005 levels.
** For this table, the revenues attributable to the proposed changes to the gross income tax and the sales tax are included in the "Tax Changes" total. For a full list of those proposed changes, see Figure 9.*

Figure 4 presents the Executive's FY 2006 revenue estimates as presented in the Governor's Budget Recommendation and the OLS's forecast. Highlights of the revenue estimates include:

FY 2006 Executive:

- The Executive expects total revenues to grow by $116 million, or 0.4% over FY 2005 (reflecting the non-recurrence of last year's securitizations).
- The estimate for the income tax is up $465 million, or 5.1% over FY 2005.
- The estimate for the sales tax is up $330 million, or 5.1% over FY 2005.
- The estimate for the corporation business tax is down $7 million, or -0.3% from FY 2005.
- The estimate for the realty transfer fee is up $60 million, or 17.4% over FY 2005.
- The Executive's revenues include $1.26 billion in new revenues requiring legislation.

FY 2006 Office of Legislative Services:

- The OLS's total revenue estimates for FY 2006 are $200 million above the Executive's projection.
- The OLS estimate for the income tax is $140 million higher than the Executive.
- The OLS estimate for the sales tax is the same as the Executive.
- The OLS estimate for the corporation business tax is the same as the Executive.
- The OLS estimate for the realty transfer fee is $50 million higher than the Executive.
- The OLS assumes the realization of proposed new revenues for comparability purposes.

Budgetary Impact of the OLS Revenue Estimates

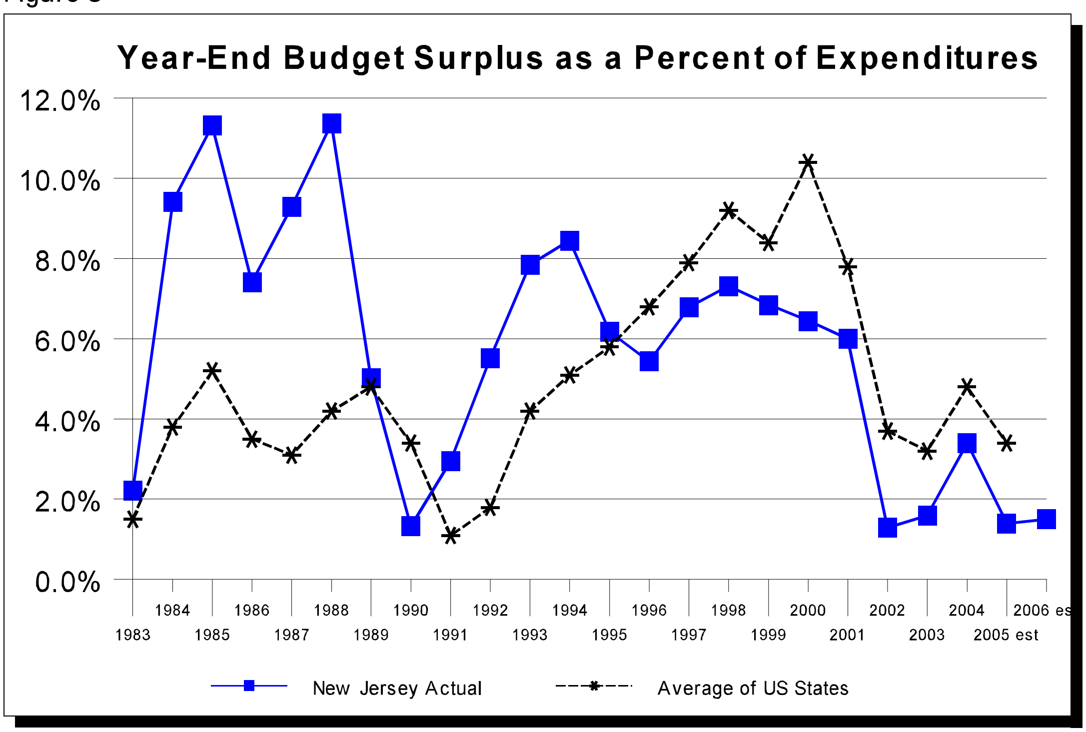
The OLS estimates FY 2005 revenues will be $87 million above the Executive projections and FY 2006 revenues will be $200 million above the Executive projections. Combined over the two year period, the OLS estimates $287 million more than the Executive.

The Executive estimates an FY 2006 year-end balance of $401 million, or about 1.5% of budgeted expenditures. As is shown in Figure 5, the proposed 1.5% surplus in FY 2006 is low by historical standards for New Jersey. Over the last quarter century, the State's surplus has generally fallen to 2% or less during economic recessions (1983, 1990, and 2002), but the State's recent structural budget problems have resulted in a series of low year-end balances. The 1.5% balance is also lower than that of the national average of all states, based on survey data compiled by the National Association of State Budget Officers.

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. All other things being equal, the higher OLS revenue estimates would produce a year-end balance of $688 million, $287 million more than the Executive's estimates. Such a potential surplus would equal about 2.5% of expenditures.

However, this calculation assumes that the spending plan and tax law changes in the FY 2006 Executive budget will be followed. The actual balance will be determined by numerous spending decisions as well as revenue collections. Decisions on these and other matters will be made by the Executive, both budget committees and the full Legislature during the next three months and throughout the fiscal year.

Figure 5



Gross Income Tax

Gross income tax (GIT) revenues will rise to new heights in FY 2005 and FY 2006, surpassing the previous peak reached three years ago. Underlying growth is solid, and last year's marginal tax rate increase (from 6.37% to 8.97% on income over $500,000) is providing a sizeable boost. These two factors combine for an estimated 23% growth to $9.1 billion in FY 2005. In FY 2006, growth should return to a more typical 7.6%, yielding $9.79 billion.

The most noteworthy aspect of the FY 2005 GIT estimate is the impact of the tax rate change on high-income taxpayers. Originally, Treasury had anticipated $830 million in new revenue. The Treasury has revised this estimate upward to $1.075 billion in FY 2005 and is projecting $991 million in FY 2006.

The FY 2006 decline in the tax change amount is due to a one-time $230 million windfall in FY 2005. This windfall occurs because the new tax rate, enacted in July 2004, was applied to income earned since January 1, 2004. Additional tax revenue that would have been collected in FY 2004 provides FY 2005 with a bonus which will not recur in FY 2006. The OLS believes the Treasury's estimates for the tax change and the one-time windfall are reasonable.

Figure 6

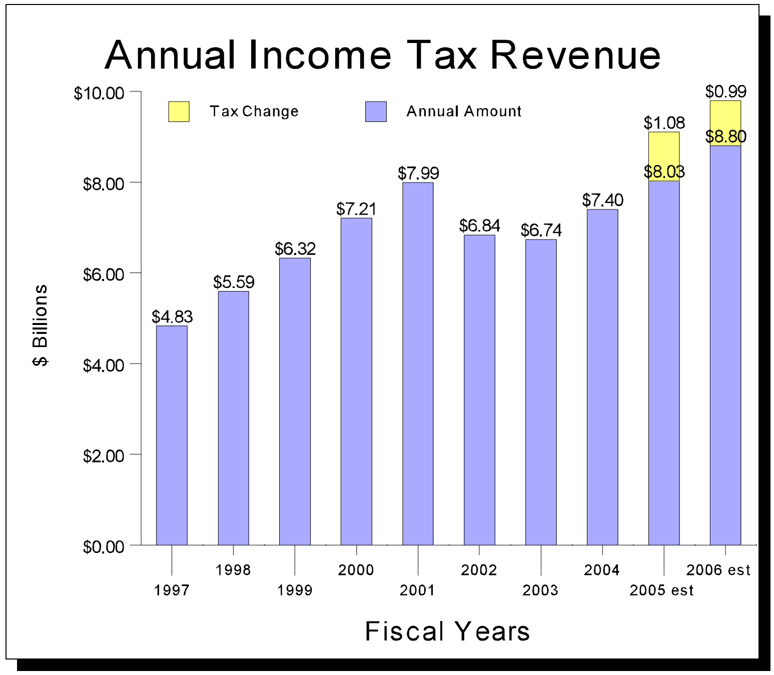
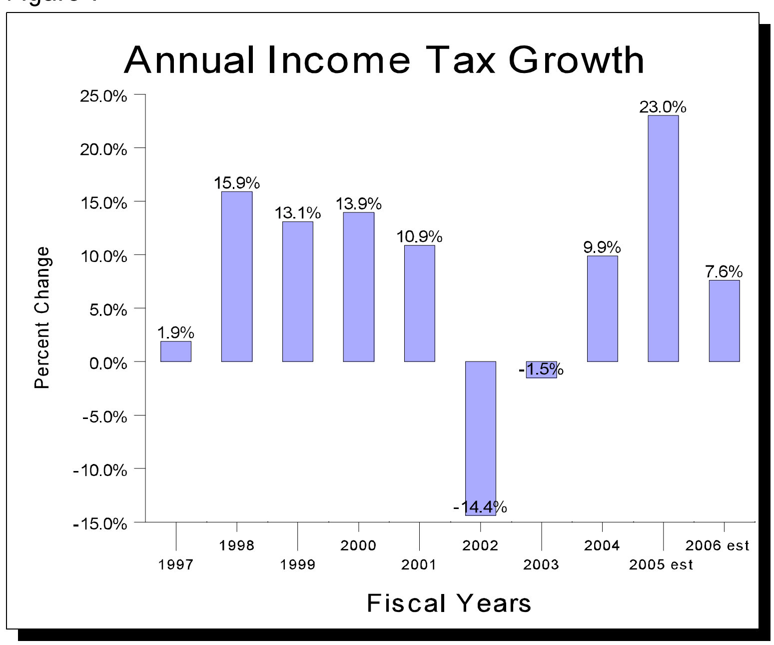


Figure 7



FY 2005: The Executive projects $9.055 billion in FY 2005, or 22.4% growth over FY 2004. The OLS estimates somewhat higher revenues of $9.1 billion, a 23.0% growth rate.

The OLS estimate is $45 million above the Executive's. This difference 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.

Gross Income Tax (Continued)

FY 2006: The Executive is estimating $9.65 billion in GIT revenue for FY 2006, an increase of 6.6% over FY 2005. The OLS is estimating $9.79 billion, or 7.6% growth over a higher FY 2005 base amount. The OLS's total is $140 million greater than the Executive's total.

Both estimates reflect the loss of the one-time windfall that occurred in FY 2005, which effectively holds down the net growth. Both estimates also include $130 million in new revenues from proposed tax changes. The Executive is proposing to limit the existing property tax deduction to taxpayers with incomes below $200,000, generating an additional $85 million. A second Executive proposal would limit the current retirement/pension exclusion to taxpayers with incomes below $100,000, generating $45 million in new revenues. Should these proposed changes be enacted, the OLS believes that the Executive's estimates of their value are reasonable.

> The recent tax rate increase is estimated to bring in $1.075 billion in FY 2005, but about $230 million of that is a one-time windfall that will not recur in FY 2006.

GIT in More Detail: Components Underlying the Estimates

In analyzing the GIT, the OLS looks 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. This is the largest component of income tax collections. Withholding receipts are up 10.4% so far in FY 2005. The OLS believes solid growth will continue in FY 2005 and FY 2006.

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 are up by nearly 48% through the first two payments of FY 2005. This extraordinary growth is largely a function of the new 8.97% marginal tax rate on incomes over $500,000. The OLS is estimating 45% growth for the rest of FY 2005, and a return to a more typical 9% growth in FY 2006.

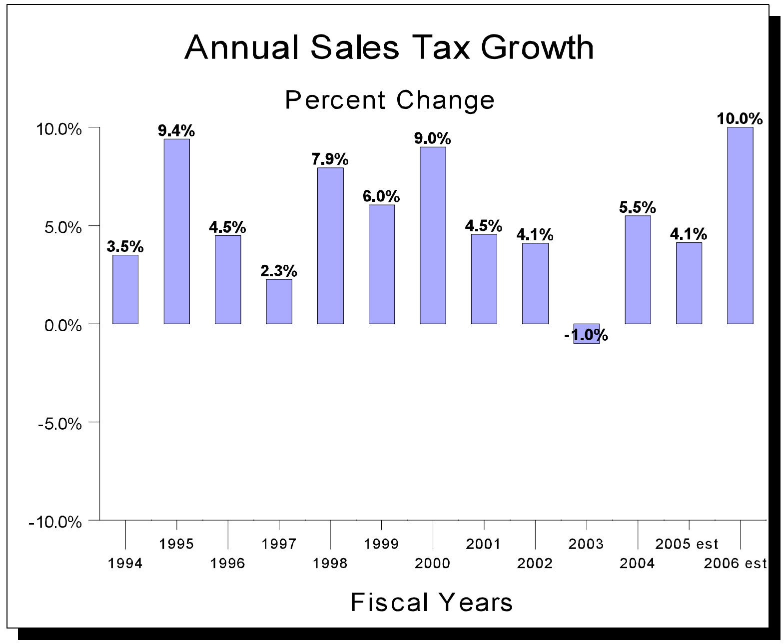
Final Payments: The linchpin for any GIT estimate is the important final tax payments that come in during April and May. As with estimated payments, taxpayers who must make large final tax payments generally have significant sources of non-wage income. The OLS believes final payments will show a significant 45% increase in FY 2005, as suggested by the strong increase in the most recent quarterly estimated payments. The OLS believes this growth will fall back to 9% in FY 2006.

Refund Payments: Refund payments are paid by the State, largely in the spring and summer, to taxpayers whose tax returns show payments exceeding their tax liability. The OLS believes refund payments will be relatively flat in FY 2005 due to the recent tax rate increase and will grow by 9% in FY 2006.

Sales Tax

The sales tax provides nearly one quarter of the State's budgeted revenues, second only to the gross income tax. In contrast to the more volatile income tax, the sales tax is rather stable, with growth rates in a narrower range. The long-term average growth rate, excluding changes in the tax rate or base, is about 5% per year.

Figure 8



FY 2005: Sales tax collections through the end of February are running 4.2% ahead of the same period one year ago. The Executive expects this growth to continue for the remainder of the fiscal year. Total collections are estimated at \$6.52 billion. The OLS believes the Executive's estimate is reasonable, based on a review of historical collection patterns and current trends.

FY 2006: The Executive expects underlying sales tax growth to increase modestly to about 5.1% in FY 2005, closer to long-term average growth. In addition, the Executive is proposing two tax changes worth a combined \$325 million. In combination with underlying growth, the tax changes are expected to increase revenues to \$7.175 billion, or 10% over FY 2005 levels.

The largest of the two proposed tax changes involves an expansion, or "modernization" of the sales tax base. As services become an increasing proportion of the State economy, the Executive is proposing to expand the sales tax to include more services. At this time, the specific services to be affected have not been revealed. However, the Executive is anticipating this proposal can yield \$275 million if in place for some portion of FY 2006.

The second proposed tax change involves the Urban Enterprise Zone (UEZ) program, worth an estimated \$50 million. The primary source of this new revenue would be a reduced UEZ sales tax exemption for qualified business purchases.

The OLS agrees with the Executive's assumption that underlying sales tax growth will return to the longer-term historical average in FY 2006. In addition, for comparison purposes, the OLS assumes the Executive's proposed tax changes will be adopted and yield the anticipated amounts. The OLS will provide independent analysis of these proposals when specific legislation is introduced.

Cigarette Tax

The Executive is estimating \$636 million on-budget from the cigarette tax in FY 2005, and \$612 million on-budget in FY 2006. The OLS agrees that sales have been declining in recent years, but year-to-date revenue growth (see Figure 2 on page 3) is somewhat stronger than the Executive estimates. Based on current trends, the OLS is projecting \$645 million in FY 2005 and \$626 million in FY 2006, \$9 million and \$14 million above the Executive's estimates respectively.

Corporation Business Taxes

The Executive reduced its FY 2005 estimate of corporation business tax (CBT) revenues from $2.5 billion to $2.162 billion. Collections have been running below expectations all year, so the Executive now anticipates a decline of 8.3% from the prior year's level. For FY 2006, the Executive anticipates a continuing decline in the CBT to $2.155 billion, including an anticipation of $29.1 million in revenues from energy-producing companies coming on budget.

The OLS agrees that FY 2005 CBT revenues have been under-performing expectations. The Executive's FY 2005 estimate is reasonable given current trends and historical collection patterns. The OLS also concurs with the Executive's projection for FY 2006.

Assessing the full impact of the Business Tax Reform Act of 2002 and understanding associated CBT revenue collection patterns is not possible until the Division of Taxation collects and releases more data from tax returns.

The OLS is projecting lower revenues than the Executive for the much smaller CBT on banks and financial institutions. This tax revenue has fluctuated from year to year, and current trends are sharply downward. The Executive reduced its estimate for FY 2005 to $85 million, a 40% drop from last year. However, through the end of February, this revenue is actually down by 58%. Based on these trends and historical patterns, the OLS is estimating $70 million in FY 2005, down 51%, and $15 million below the Executive.

In FY 2006 the Executive is estimating flat CBT banks and financial institutions revenue of $85 million. The OLS agrees with the cautious approach and is accordingly estimating a flat $70 million in FY 2006, $15 million below the Executive.

Realty Transfer Fee

The realty transfer fee has grown significantly in recent years. In Fiscal Years 2000 and 2001, this fee brought in $78 and $79 million respectively for the State budget. But, in FY 2004, it raised $227 million, and the Executive is expecting $345 million in FY 2005 and $405 million in FY 2006. These sharp increases are due to a combination of multiple increases in the fees and an on-going boom in home sales encouraged by historically low interest rates. These factors are discussed in greater detail in the appendix of this report.

The OLS is even more optimistic about realty transfer fee revenue than is the Executive. In FY 2005, growth is running at nearly 74% above last year through the end of February. The fee increases enacted last year would account for about two-thirds of the growth, with growth in sales and home values accounting for the rest. The Executive's FY 2005 estimate of $345 million implicitly assumes market-driven growth will decline for the remainder of the fiscal year, bringing total growth down to about 52%. The OLS does not expect such a sharp change in the home sales market and is therefore estimating $390 million in FY 2005, 72% above last year, and $45 million above the Executive's estimate.

The OLS agrees with the Executive that growth should moderate as we move into FY 2006. The OLS is estimating $455 million for next fiscal year, about 17% growth, and $50 million above the Executive's estimate. The Executive and OLS revenues include a tax rate change worth an estimated $25 million.

The OLS is also estimating more revenue from the new, separate tax on homes worth over $1 million. The Executive estimates $44 million in FY 2005 and $48 million in FY 2006. The OLS estimates $48 million in FY 2005 based on current trends, and $60 million in FY 2006, reflecting the State's receipt of a full year's collection from this new tax.

Revenue Changes Requiring Legislation

Figure 9 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.

Figure 9

Certain FY 2006 Revenue Changes Requiring Legislation

($ Millions)

Revenue Source	Estimated Amount	Comment/Details
Income Tax - Limit Property Tax Deduction	$85.0	Allow current property tax deduction under the income tax only for taxpayers with less than $200,000 income. Affects 9.4% of taxpayers who claim the deduction.
Income Tax - Pension Exclusion	$45.0	Allow current retirement income exclusion (up to $20,000) only for taxpayers with less than $100,000 income. Affects 5.7% of taxpayers who use the exclusion.
		Income Tax Sub Total = $130.0 million
Sales Tax - Expansion ("Modernization") of base	$275.0	Proposal will recommend the inclusion of certain services in the sales tax base. Suggested possibilities include: shipping/handling, limousine services, luxury box rentals, charter airplane services, tanning, massages, and landscaping.
Sales Tax - UEZ Reforms	$50.0	Lower UEZ business exemption from 6% to 3%; require businesses to pay 6% up front and apply for 3% refunds.
		Sales Tax Sub Total = $325.0 million
Asset Sales	$500.0	Unspecified sales of State assets. Executive reports the State has $19.4 billion in assets.
Video Lottery Terminals	$150.0	Beginning in January of 2006, the Meadowlands complex would host video lottery terminals. The initial revenue projection is for 6 months.
Cable Industry Gross Receipts Tax	$50.0	A 2% gross receipts tax on cable television.
Simplified Sales Tax Implementation/Amnesty	$40.0	A one-year voluntary amnesty, under the pending multi-state compact for the streamlined sales tax structure, for companies that have enough activity in New Jersey to be required to collect sales tax but have not yet registered to do so.
Transfer Inheritance Tax	$25.0	Unspecified changes to the State tax designed to capture certain revenues from taxpayers benefiting from federal estate tax changes.

Figure 9
Certain FY 2006 Revenue Changes Requiring Legislation
($ Millions)

Revenue Source	Estimated Amount	Comment/Details
Realty Transfer Fee	$25.0	Increases realty fee rates on the sale of properties between $150,000 and $350,000.
Fines Amnesty	$15.0	Waives interest for certain delinquent fines, fees, and assessments of individuals and businesses.
		Other Sub Total = $805.0 million
Total, FY 2006	$1,260.0	

Appendix Contents:

Detailed Fiscal Year 2005 Revenue Estimates
$ Millions

Revenue Source	Approp. Act	Executive Revised	OLS	Diff: OLS - Executive
Major Taxes:				
Sales Tax, Total	$6,600.0	$6,520.0	$6,520.0	$0.0
Corporation Business Tax, Total	2,500.0	2,162.0	2,162.0	0.0
Corporation Business Tax, Energy Contribution	*0.0*	*0.0*	*0.0*	*0.0*
Motor Fuels	559.0	565.0	565.0	0.0
Motor Vehicle Fees	301.1	272.0	272.0	0.0
Inheritance Taxes	556.0	500.0	500.0	0.0
Insurance Premiums	449.0	432.0	432.0	0.0
Cigarette	678.0	636.0	645.0	9.0
Petroleum Products Gross Receipts	212.0	250.0	250.0	0.0
Corporation Business - Banks and Financial	132.0	85.0	70.0	(15.0)
Alcoholic Beverage Excise	88.0	87.0	87.0	0.0
Realty Transfer	286.0	345.0	390.0	45.0
Tobacco Products Wholesale	10.0	12.0	12.0	0.0
Public Utilities Excise	8.7	9.0	9.0	0.0
Subtotal, Major Taxes	$12,379.8	$11,875.0	$11,914.0	$39.0
Misc. Taxes, Fees and Revenues				
Assessment on Homes Valued Over $1 Million	$24.0	$44.0	$48.0	$4.0
Transitional Energy Facility Assessments	222.2	221.9	221.9	0.0
Medicaid Uncomp. Care Reimbursement	529.9	440.3	440.3	0.0
Telephone Assessment	118.0	115.0	115.0	0.0
Hotel Occupancy Tax	65.1	65.1	65.1	0.0
Other	1,595.5	1,647.8	1,647.8	0.0
Subtotal, Misc. Revenues	$2,554.7	$2,534.1	$2,538.1	$4.0
Interfund Transfers				
State Lottery Fund	$795.0	$800.0	$800.0	$0.0
Cigarette Tax and MV Securitizations	1,930.0	1,930.0	1,930.0	0.0
Unclaimed Personal Property Trust Fund	194.1	194.1	194.1	0.0
Other	350.2	355.2	355.2	0.0
Subtotal, Interfund Transfers	$3,269.3	$3,279.3	$3,279.3	$0.0
TOTAL GENERAL FUND	$18,203.7	$17,688.3	$17,731.3	$43.0
Property Tax Relief Fund (Income Tax), Total	$8,855.0	$9,055.0	$9,100.0	45.0
Income Tax, Base	*8,025.0*	*7,980.0*	*8,025.0*	*45.0*
Income Tax, Tax Changes	*830.0*	*1,075.0*	*1,075.0*	*0.0*
Casino Revenue Fund	474.9	482.2	482.2	0.0
Casino Control Fund	65.6	69.6	69.6	0.0
Gubernatorial Elections Fund	1.5	1.5	0.7	(0.8)
GRAND TOTAL, ALL FUNDS	$27,600.7	$27,296.6	$27,383.8	$87.2

Detailed Fiscal Year 2006 Revenue Estimates
$ Millions

Revenue Source	Executive	% Change	OLS	% Change	Diff: OLS - Executive
Major Taxes:					
Sales Tax, Total	$7,175.0	10.0%	$7,175.0	10.0%	$0.0
Sales Tax, Base	*6,850.0*	*5.1%*	*6,850.0*	*5.1%*	*0.0*
Sales Tax, Proposed Tax Changes	*325.0*	--	*325.0*	--	*0.0*
Corporation Business Tax, Total	2,155.1	(0.3)%	2,155.1	(0.3)%	0.0
Corporation Business Tax, Base	*2,126.0*	*(1.7)%*	*2,126.0*	*(1.7)%*	*0.0*
Corporation Business Tax, Energy Contribution	*29.1*	--	*29.1*	--	*0.0*
Motor Fuels	580.0	2.7%	580.0	2.7%	0.0
Motor Vehicle Fees	294.3	8.2%	294.3	8.2%	0.0
Inheritance Taxes	545.0	9.0%	545.0	9.0%	0.0
Inheritance Taxes, Base	*520.0*	*4.0%*	*520.0*	*4.0%*	*0.0*
Inheritance Taxes, Proposed Tax Change	*25.0*	--	*25.0*	--	*0.0*
Insurance Premiums	443.0	2.5%	443.0	2.5%	0.0
Cigarette	612.0	(3.8)%	626.0	(2.9)%	14.0
Petroleum Products Gross Receipts	255.0	2.0%	255.0	2.0%	0.0
Corporation Business - Banks and Financial	85.0	0.0%	70.0	0.0%	(15.0)
Alcoholic Beverage Excise	91.0	4.6%	91.0	4.6%	0.0
Realty Transfer	405.0	17.4%	455.0	16.7%	50.0
Tobacco Products Wholesale	12.0	0.0%	12.0	0.0%	0.0
Public Utilities Excise	9.0	0.0%	9.0	0.0%	0.0
Subtotal, Major Taxes	$12,661.4	6.6%	$12,710.4	6.7%	$49.0
Misc. Taxes, Fees and Revenues					
Assessment on Homes Valued Over $1 Million	$48.0	9.1%	$60.0	25.0%	$12.0
Transitional Energy Facilities Assessment	235.0	5.9%	235.0	5.9%	0.0
Medicaid Uncomp. Care Reimbursement	466.1	5.9%	466.1	5.9%	0.0
Telephone Assessment	119.0	3.5%	119.0	3.5%	
Hotel Occupancy Tax	65.1	0.0%	65.1	0.0%	0.0
New Revenues and Asset Sales	605.0	--	605.0	--	0.0
Other	1,601.1		1,601.1		0.0
Subtotal, Misc. Revenues	$3,139.3	23.9%	$3,151.3	24.2%	$12.0
Interfund Transfers					
State Lottery Fund (Current Law)	$820.0	2.5%	$820.0	2.5%	$0.0
Proposed Video Lottery Terminals (State Lottery)	150.0	--	150.0	--	0.0
Unclaimed Personal Property Trust Fund	194.1	0.0%	194.1	0.0%	0.0
Other	240.0		240.0		0.0
Subtotal, Interfund Transfers	$1,404.1	(57.2)%	$1,404.1	(57.2)%	$0.0
TOTAL GENERAL FUND	$17,204.8	(2.7)%	$17,265.8	(2.6)%	$61.0
Property Tax Relief Fund (Income Tax), Total	$9,650.0	6.6%	$9,790.0	7.6%	140.0
Income Tax, Base	*9,520.0*	*5.1%*	*9,660.0*	*6.2%*	*140.0*
Income Tax, Proposed Tax Changes	*130.0*	--	*130.0*	--	*0.0*
Casino Revenue Fund	487.2	1.0%	487.2	1.0%	0.0
Casino Control Fund	69.6	0.0%	69.6	0.0%	0.0
Gubernatorial Elections Fund	1.5	0.0%	0.7	0.0%	(0.8)
GRAND TOTAL, ALL FUNDS	$27,413.1	0.4%	$27,613.3	0.8%	$200.2

Public Utility Tax Revenue

Energy utilities in New Jersey are 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 are subject to the CBT. The revenues are divided into two categories: Municipal Use, which are "off budget" and State Use, which are "on budget."

Figure 1 below displays public utility revenues between FY 1991 and FY 2006. (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 2003 and FY 2006 in greater detail.

From a budgeting perspective, the *municipal use* tax revenues are credited to the Energy Tax Receipts Property Tax Relief Fund, are considered "off budget", and are allocated to municipalities under a statutory formula. These amounts are not included in either the anticipated revenues or the amount of State aid appropriated in the annual appropriations act. This amount has grown to an estimated $787.8 million in FY 2005 and is expected to increase slightly to $788.5 million in FY 2006.

The "on budget" *State use* portion consists primarily of TEFA revenue. TEFA was originally scheduled to end in FY 2002. However, P.L. 2001, c.433, extended the assessment through FY 2006. Then, P.L. 2004, c.43, further extended the TEFA. Payments are now scheduled to phase down beginning in FY 2007 and the final payments will be received in FY 2010. The Executive is estimating TEFA payments of $221.9 million in FY 2005 and $235 million in FY 2006. Total on budget energy collections are estimated at $307.8 million in FY 2005 and $350.1 million in FY 2006.

Figure 1

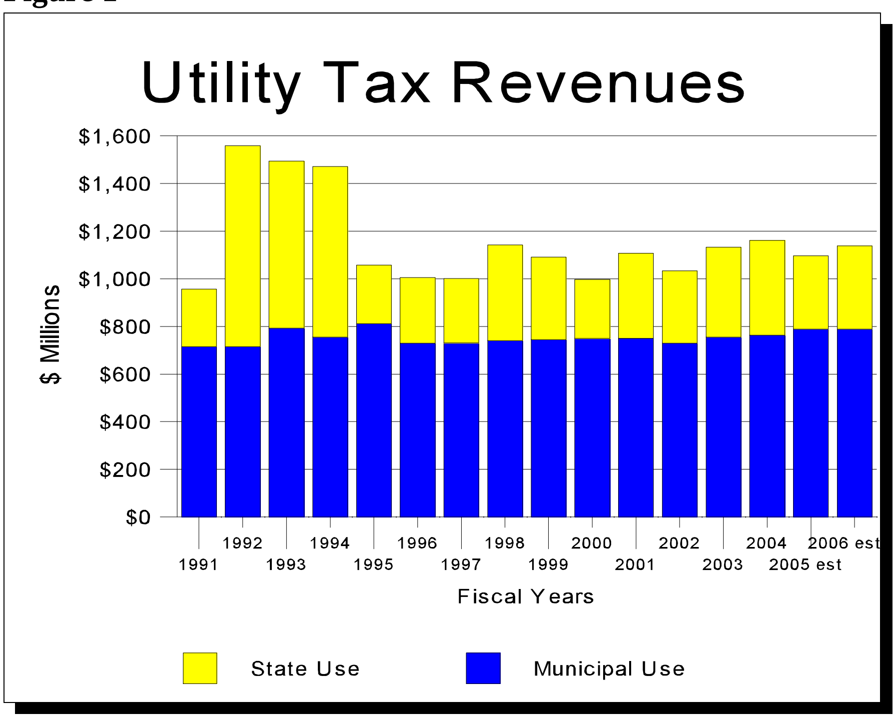


Figure 2
Actual Public Utility Tax Revenue Fiscal Year 2003
($ Millions)

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 3
Actual Public Utility Tax Revenue Fiscal Year 2004
($ Millions)

Revenue Source	On-Budget (State Use)	Off-Budget (Municipal Aid)	Total
Sales and Use Tax	$27.9	$686.1	$714.0
Corporation Business Tax	$33.1	$76.6	$109.7
Transitional Energy Facilities Assessment (TEFA)	$249.5		$249.5
Customer Specific Tax	$1.9		$1.9
Franchise and Gross Receipts Tax Water and Sewer Utilities	$76.9		$76.9
Public Utility Excise Tax Water and Sewer Utilities	$9.3		$9.3
Total	$398.6	$762.7	$1,161.3

Source: Department of Treasury, March 2005.

Figure 4
Anticipated Public Utility Tax Revenue Fiscal Year 2005
($ Millions)

Revenue Source	On-Budget (State Use)	Off-Budget (Municipal Aid)	Total
Sales and Use Tax		$720.4	$720.4
Corporation Business Tax		$49.5	$49.5
Transitional Energy Facilities Assessment (TEFA)	$221.9	$17.9	$239.8
Customer Specific Tax	$1.9		$1.9
Franchise and Gross Receipts Tax Water and Sewer Utilities	$75.0		$75.0
Public Utility Excise Tax Water and Sewer Utilities	$9.0		$9.0
Total	$307.8	$787.8	$1,095.6

Source: Department of Treasury, March 2005.

Figure 5
Anticipated Public Utility Tax Revenue Fiscal Year 2006
($ Millions)

Revenue Source	On-Budget (State Use)	Off-Budget (Municipal Aid)	Total
Sales and Use Tax		$732.6	$732.6
Corporation Business Tax	$29.1	$55.9	$85.0
Transitional Energy Facilities Assessment (TEFA)	$235.0		$235.0
Customer Specific Tax	$2.0		$2.0
Franchise and Gross Receipts Tax Water and Sewer Utilities	$75.0		$75.0
Public Utility Excise Tax Water and Sewer Utilities	$9.0		$9.0
Total	$350.1	$788.5	$1,138.6

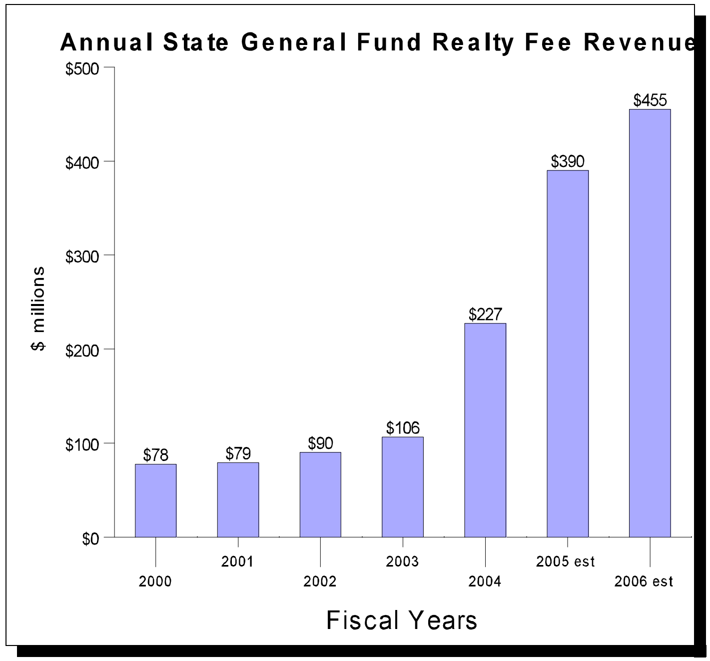
Source: Department of Treasury, March 2005.

The Recent Surge in Realty Transfer Fee Revenue

A booming real estate market and fee increases in three consecutive years will have more than quadrupled the State's realty transfer fee collections in support of the General Fund from Fiscal Year 2003 to Fiscal Year 2006, according to the forecast by the OLS. The fee would thus become the 7th most significant State revenue raiser in FY 2006 after being just the 11th largest in FY 2003.

All the numbers presented in this appendix exclude the fee in the amount of one percent of the transaction price on the buyer of residential real property acquired for $1 million or more. In effect since August 1, 2004, this fee is accounted for separately from the realty transfer fee.

Figure 6



Under current law, the seller of real property pays the realty transfer fee upon the recording of the change in title. The specific amount owed depends on the selling price to which the county recording officer applies the appropriate graduated rate schedule. Two schedules exist: one for properties sold for $350,000 or less and one for properties sold for more than $350,000. In addition, reduced rate schedules pertain to properties that are either sold by a senior, blind or disabled resident or that qualify as low or moderate income housing.

The State and its counties share the fee proceeds. In FY 2004, the counties received $100 million in fee revenue and the State collected $297 million, of which $227 million supported its General Fund and $70 million the Neighborhood Preservation Nonlapsing Revolving Fund. From the General Fund collections, the first $25 million are dedicated to the Shore Protection Fund and the next $12 million to the Highlands Protection Fund.

In FY 2003, the fee's State General Fund collections were about $106 million. One year later, that amount more than doubled to $227 million and the OLS forecasts it to grow to $455 million in FY 2006. Figure 6 depicts the actual and projected increase in the fee's State General Fund proceeds since FY 2000. Two factors largely explain this revenue quadrupling over three years: rate increases and a boom in the New Jersey real estate market.

Statutory rate increases went into effect in each of FY 2004 and FY 2005 and the Executive FY 2006 budget proposes another rate expansion. The FY 2006 expansion would extend only to properties sold for more than $150,000 but no more than $350,000, following the FY 2005 increase, which applied only to properties sold for more than $350,000. Figure 8 details the progression of the standard realty transfer fee from a two-tiered fee in FY 2003 to two different rate schedules in FY 2005, one with six tiers for properties selling for more than $350,000 and another one with three tiers for properties selling for up to $350,000. The table also includes the FY 2006 rate schedule proposed by the Executive, which would increase the fees associated with each of the three tiers for properties selling for more than $150,000 but no more than $350,000.

The rate modifications have affected property sellers appreciably, with the heaviest impact falling on sellers of high-value properties. In FY 2003, a $5 million property transfer resulted in a fee liability of $24,775. In FY 2005, the same realty transfer results in a liability of $57,975, an increase of $33,200 or 134 percent. On the other hand, a $450,000 property transfer produced a fee liability of $2,025 in FY 2003. In FY 2005, it bears a liability of $3,695, an increase of $1,670 or 82.5 percent.

The proposed FY 2006 realty fee changes would not impact the previous examples. However, the proposal would apply to a $300,000 property transfer, whose fee liability was $1,275 in FY 2003, $1,715 in FY 2005, and would increase under the Executive proposal to $2,200 in FY 2006. Over FY 2003, this change would represent an increase of $925 or 72.5 percent.

The boom in the real estate market, propelled in part by record low mortgage rates, has been the second major contributor to the marked upswing in realty transfer fee revenue. According to the New Jersey Association of Realtors, the price of the median resold home in New Jersey has grown from $186,700 in 2000 to $301,675 in 2004, a growth of 61.6 percent. Simultaneously, the sales volume of resold homes has risen by 18.1 percent from 134,400 units in 2000 to 158,700 units in 2004. Realty transfer fee collections reflect this boom.

Exclusive of the revenue portion generated by the recent statutory changes, State General Fund fee proceeds will increase from $106 million in FY 2003 to $190 million in FY 2006. This growth of $84 million, or 79 percent, is solely attributable to the growth in in the real estate market.

Figure 7

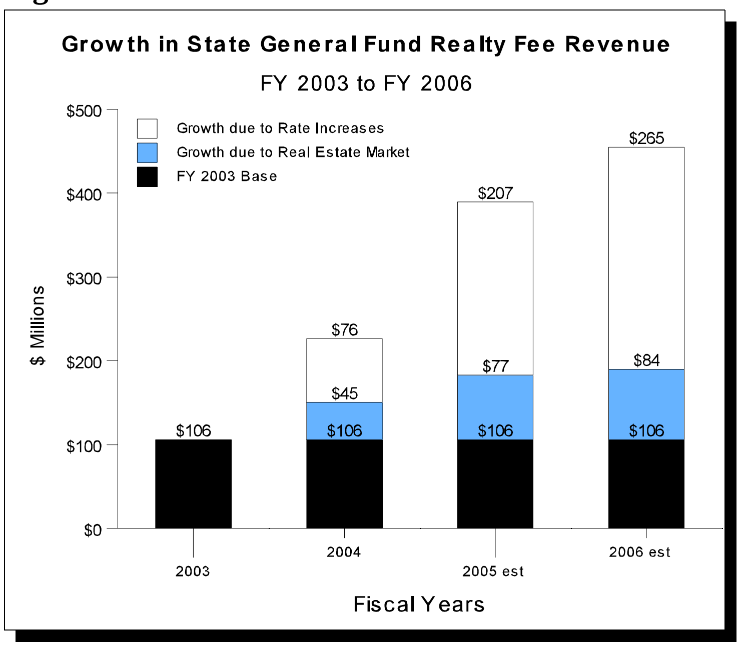


Figure 7 shows which part of the $339 million growth in the State General Fund fee revenue between FY 2003 and FY 2006 is attributable to the rate expansion and which is a consequence of developments in the real estate market. All of the fee increases from FY 2003 through FY 2006 are forecast to contribute a cumulative $265 million to the State General Fund, or 76 percent of the projected $339 million increase. The real estate market, on the other hand, is forecast to account for $84 million, or 24 percent, of the projected $339 million increase.

Figure 8
Realty Transfer Fee Rate Structure Since FY 2003

(Levied per $500 of the selling price recited in the deed that fall within each bracket)

<table>
<tr><th>Real Property Sold</th><th>Bracket</th><th colspan="2">FY 2003</th><th>FY 2004</th><th>FY 2005</th><th>Executive FY 2006 Proposal</th></tr>
<tr><td></td><td>Construction Type</td><td>Existing</td><td>New</td><td>Existing and New</td><td>Existing and New</td><td>Existing and New</td></tr>
<tr><td rowspan="6">Over $350,000</td><td>first $150,000</td><td>$1.75</td><td>$0.75</td><td>$2.00</td><td>$2.90</td><td>$2.90</td></tr>
<tr><td>$150,000 to $200,000</td><td rowspan="5">$2.50</td><td rowspan="5">$2.50</td><td>$3.35</td><td>$4.25</td><td>$4.25</td></tr>
<tr><td>$200,000 to $550,000</td><td rowspan="4">$3.90</td><td>$4.80</td><td>$4.80</td></tr>
<tr><td>$550,000 to $850,000</td><td>$5.30</td><td>$5.30</td></tr>
<tr><td>$850,000 to $1,000,000</td><td>$5.80</td><td>$5.80</td></tr>
<tr><td>over $1,000,000</td><td>$6.05</td><td>$6.05</td></tr>
<tr><td rowspan="3">More than $150,000 up to $350,000</td><td>first $150,000</td><td>$1.75</td><td>$0.75</td><td>$2.00</td><td>$2.00</td><td>$2.75</td></tr>
<tr><td>$150,000 to $200,000</td><td rowspan="2">$2.50</td><td rowspan="2">$2.50</td><td>$3.35</td><td>$3.35</td><td>$4.25</td></tr>
<tr><td>$200,000 to $350,000</td><td>$3.90</td><td>$3.90</td><td>$4.75</td></tr>
<tr><td>Up to $150,000</td><td>up to $150,000</td><td>$1.75</td><td>$0.75</td><td>$2.00</td><td>$2.00</td><td>$2.00</td></tr>
</table>

Notes:
1. In FY 2004, the distinction between existing and new construction was discontinued.
2. In FY 2005, a distinction between real property sold for up to $350,000 and real property sold for over $350,000 was introduced.
3. A different rate schedule applies to real property sold by senior, blind, and disabled residents as well as to sales of low and moderate income housing.
4. In FY 2005, a fee in the amount of 1 percent of the selling price recited in the deed was imposed on the buyer of residential real property sold for $1,000,000 or more. This table does not include this fee.

New Jersey Review and Economic Outlook for 2005-2006

State of New Jersey
Council of Economic Advisors
February 2005

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 2005-2006 Revenue Analysis.

New Jersey Economic Review & Outlook For 2005-2006

Forecast Summary "New Jersey's economy has outperformed the national economy for six straight years and is likely to keep that streak alive in 2005."

Dr. Joseph J. Seneca, Chairman **February 2005**

New Jersey Forecast 2005 –2006

The New Jersey economy had a breakout year in 2004 after struggling for three years in the context of a weak national economy. Indeed, as detailed later in this review, New Jersey's economy was one of the best performing in the nation. Employment increased by 75,900 jobs, or by 1.9%, from December 2003 through December 2004. This strong performance stands in sharp contrast to the state's meager 0.6% increase in 2003 and job declines of -0.4% and -0.8% in the two previous years. With almost all of the state's employment sectors showing gains in the last year, New Jersey has strong economic momentum going into 2005.

Summary: New Jersey Forecast (% Change)		
	2005	2006
Gross State Product (Current $, bill)	4.6%	4.3%
Personal Income (Current $, bill)	4.7%	3.5%
Retail Sales (Current $, bill)	4.1%	3.2%
Consumer Price Index (All Urban)	3.2%	2.7%
Total Non-Ag Employment	1.4%	1.1%

The outlook for 2005 is for continued, but moderating, growth. The state's export and transportation and warehousing sectors will benefit from the decline in the dollar as the volume of international trade expands. Solid increases in national capital spending on computer equipment and software will assist the state's long-suffering technology sector. Leisure and tourism will benefit from steady gains in income and employment. Pharmaceuticals and biotechnology, supported by long-term demographic trends of a large and now aging baby boom generation, remains a cornerstone of New Jersey's high technology economy. But relentless competition, legal problems, and possible changes in federal regulatory oversight will keep cost pressures on the industry.

New Jersey's red-hot residential construction and existing home markets will cool as rising mortgage rates and constraints on building sites reduce both demand and supply. High vacancy rates for office space, despite record levels of employment in New Jersey, will reduce commercial construction's contribution to growth in 2005.

Consumers will continue to do the heavy economic lifting in 2005 supported by gains in employment and income. However, high levels of consumer debt, the end of federal income tax cuts, and significantly higher energy costs since last year will constrain increases in consumer spending.

A high federal deficit and a second term administration in Washington with a focus on tighter spending controls dampens the prospect for any boost for the state from the federal budget. The state's high technology sector, which has benefited from federal defense and homeland security spending, will be hard pressed to receive the same level of federal spending in 2005 as last year.

Manufacturing showed signs of stabilizing in 2004 as the employment decline in this long-battered sector moderated. However, the sector remains under intense pressure from lower cost competitors across the country and the globe.

The end of federal depreciation tax incentives for investment spending is another factor contributing to slower growth in 2005. Continuing improvements in the New York City economy after another good year in the capital markets, and from accelerating employment growth in Pennsylvania, will help regional economic activity.

The U.S. Economy

The national economy (finally!) roared to life in 2004 with strong gains in *both* real Gross Domestic Product (4.4%) and in employment (1.7%) for the first time since 2000. Growth was led by consumer spending (3.8%), residential investment (9.5%), business capital spending (13.4%), and exports (8.1%). Import growth (9.8%) and weak state and local government spending (0.4%) constrained GDP growth. Employment increases averaged 186,000 new jobs per month and, as a result, the unemployment rate drifted down to 5.4% by year's end. Total personal income rose by a robust 5.3% and the equity markets had a respectable year with the Standard and Poors 500 rising by nearly 9%. Inflation, rather than deflation, emerged as a concern as energy prices spiked and commodity prices rose in response to global demand pressures and the Consumer Price Index increased by 3.3%.

The national economy should slow in 2005 from the strong, above trend, 4.4% increase in GDP of last year as higher energy prices, rising interest rates, and the end of the federal tax cut stimulus dampen consumer spending. The red-hot housing sector, which has sustained the recovery to date, is unlikely to contribute to growth in 2005. Federal spending, after rising by 7.5% in 2002, 6.6% in 2003, and 4.7% last year, is also likely to contribute less to growth in the year ahead.

Business spending on technology should remain a positive factor since firms have large cash balances and are likely to continue to invest in technology upgrades. Exports will boost the economy again in 2005 as the dollar continues to depreciate and import growth should moderate. Given the improving economy, monetary policy will turn less accommodative as the Federal Reserve continues on its path of restoring interest rates to more historically comparable levels, as well as reducing the rate of increase in the money supply.

Payroll employment will add 2 million new jobs in 2005, a decline from the past year's pace, but still sufficient to absorb new entrants into the labor force, nudge the unemployment rate lower, and support income growth. The extraordinary increases in productivity over the last several years are now history and any growth in output must increasingly be met by new hiring. Inflation, always at the mercy of energy costs, should remain in the 3% range as increases in commodity prices and import prices, and some increased testing of pricing power by businesses contribute to general price increases.

Factors that could upset this outlook for moderating but steady growth are further energy cost spikes, terrorism, and a free-fall in the dollar. These all could result in sharp increases in interest rates and disrupt capital markets, housing, and consumer spending.

New Jersey Ranks Among the Leaders

In the past year, the national economic recovery finally took hold across the country. As of December 2004, unemployment rates had declined in 43 states compared to the previous December. Employment levels increased in 48 of the 50 states and did so in almost every sector.

Annual Employment Change by State
December 2003 - December 2004
Seasonally Adjusted, in thousands

State	Change: Dec.03-Dec.04	Rank
Florida	172.3	1
California	152.3	2
Texas	124.8	3
Virginia	79.5	4
North Carolina	76.4	5
New Jersey	**75.9**	**6**
Pennsylvania	70.5	7
Washington	64.5	8
Arizona	63.9	9
Wisconsin	63.6	10

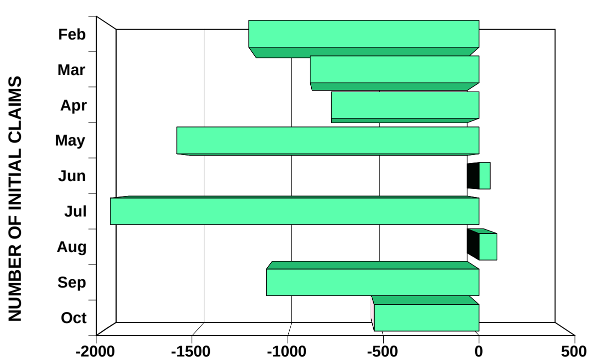
Within the broad national recovery in 2004, New Jersey stands out. Employment in New Jersey grew by 75,900 from December 2003 to December

2004 and the state ranked 6th among all states in job gains. Only the Sunbelt and southern states of Florida, California, Texas, Virginia, and North Carolina did better. New Jersey ranked ahead of all our neighbors (Pennsylvania +70,500 jobs, New York +58,500 jobs, and Connecticut +8,000 jobs). New Jersey also did well in terms of private sector job creation, ranking 10th with 58,800 new jobs.

Employment Profile

By the end of 2004 New Jersey's unemployment rate (4.2% as of December) was more than a full percentage point below that of the nation and the state's job gains were broad based. Another sign of improvement in the state's labor markets was the decline in initial unemployment claims in 2004 compared to a year ago.

Initial Claims for NJ Unemployment Insurance, Change from Year Ago



By April of 2004 New Jersey's total employment surpassed its previous peak set in December 2000 and continued to establish new records every month since. By year's end (December 2004), employment in New Jersey was 4,075,100, or 49,800 jobs higher than the previous peak. New Jersey had regained 174% of the 67,000 jobs lost during the 27-month employment decline from December 2000 to March 2003.

Overall in 2004, employment increased by 75,900 jobs, significantly above the long-term post World War II annual average of 50,000. The job gains were broad based with strong increases in education and health services (15,200), leisure and hospitality (12,500), professional and business services (10,400), finance (9,600), construction (8,200), and government (17,100). Only two sectors lost jobs. On-going instability in wired telecommunications caused employment in the information sector to decline (-700). Manufacturing continued its long run employment decline (-4,600), although the rate of loss slowed considerably from last year (-10,400).

NJ Employment % Change by Sectors, 2003-04

Sectors	Percent
Construction	**5.2%**
Leisure and Hospitality	**3.9%**
Financial Activities	**3.4%**
Educational and Health Services	**2.8%**
Government	**2.7%**
Professional & Business Services	**1.8%**
Trade, Transportation, and Utilities	**0.6%**
Information	**-0.7%**
Manufacturing	**-1.3%**
Total Non-Ag	**1.9%**

In previous Outlooks, the Council identified six business clusters that embody dynamic aspects of the New Jersey economy. Together these six clusters contain over 25% of total private sector employment in New Jersey. In 2004, employment grew in four of the six clusters, a distinct turnaround from the previous year when employment declined in four of the six clusters.

Employment in NJ Growth Clusters, Change 2003-04

	Number (000)	Percent
Finance	**2.2**	**1.6%**
Science and Technology	**0.3**	**0.2%**
Casino/Entertainment	**0.3**	**0.3%**
Pharmaceutical/Bio Tech	**0.2**	**0.3%**
Logistics	**-1.4**	**-0.5%**
Information Technology	**-2.2**	**-1.7%**
Cluster Total	**-0.5**	**-0.10%**

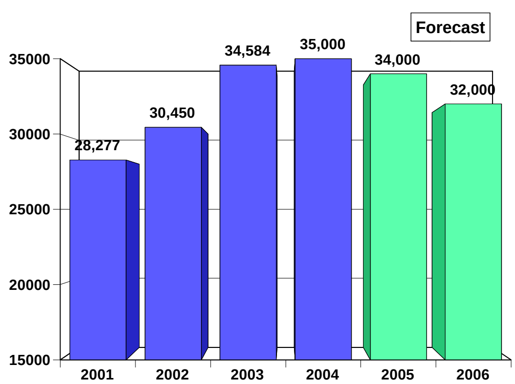
Personal Income and Consumer Spending

Total personal income grew by 4.2% in 2004 (3rd quarter 04 vs. 3rd quarter 03). Income was boosted by the state's strong employment gains and by federal tax cuts. Continuing increases in employment and increases in interest and dividend income will support income growth in 2005. Personal income is projected to rise by 4.7%.

Consumer spending faces a mixed outlook for 2005. The boost in disposable income from the federal tax cuts is now past. Rising interest rates, higher energy prices, and increases in health care costs will dampen spending. Home equity loans, which have been heavily used by households to finance spending, are likely to decline as interest rates rise. However, solid employment gains will continue to assist income and spending. As a result, consumer spending is expected to increase by 4.7% in 2005.

New residential building permits in 2004 exceeded 30,000 units for the third consecutive year. Sales of existing homes were up 7% over the already high levels of 2003. Spending on home improvements was very strong and supported large gains in retail sales for furnishings and in construction employment. Total construction employment (167,000) is near its all-time high.

NJ Residential Building Permits, No.

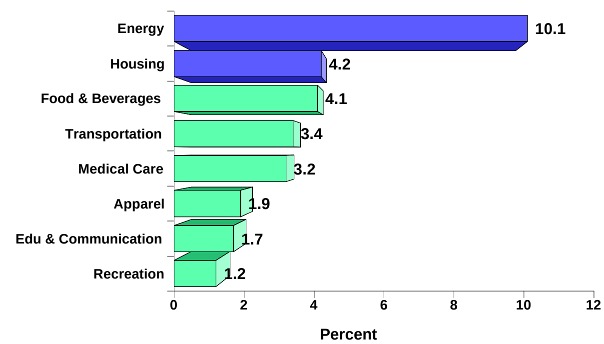


New vehicle registrations weakened in 2004 despite a series of dealer incentive offers throughout the year. Through November 2004, new registrations totaled 590,218 and were 2.9% below the comparable period a year ago. However, the level of new registrations remains high and the outlook is for new registrations to again exceed 600,000 in 2005.

Consumer Prices

Inflation, which had been dormant for many years, stirred in 2004 and prices in the New York/New Jersey metropolitan area rose by 3.5%, an acceleration from last year's pace of 3.1%. Energy price spikes in early spring and again in late summer dominated the increase (10.1%) and drained consumer spending on other goods and services (see Sidebar). Transportation costs (3.4%), food costs (4.1%), and housing costs (4.2%) also contributed to the higher inflation rate. Below average increases occurred in medical care (3.2%), apparel (1.9%), and education and communication (1.7%).

NY/NJ Consumer Price Index, by Expenditure Category, % Change 2003-04
All Items = 3.5 %



There was a surge in commodity and producer prices nationally, but these increases have only partly penetrated into the prices of final products. The decline in the dollar will continue to put upward pressures on the prices of imports. Businesses, which previously lacked pricing power due to global competition and excess capacity, may begin to explore edging prices upward. The main unknown, as always, is energy costs. Forecasts call for a stabilization and subsequent decline in energy costs this year (but that was also the consensus projection for 2004!). Accordingly, caution should prevail concerning the forecast, which calls for inflation to moderate slightly in 2005.

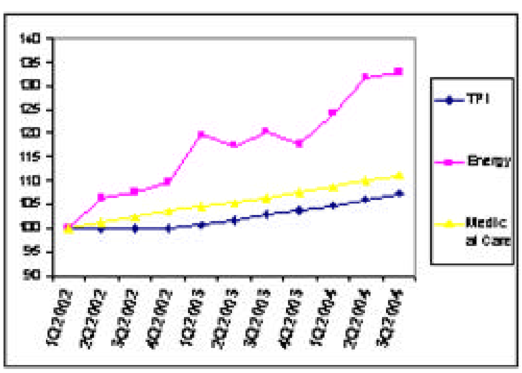
Investing in New Jersey

Energy and Medical Care Costs

The drain on consumer spending from increased energy and medical care costs has been considerable. The on-going uncertain nature of energy supplies raises the possibility of further oil price spikes given the volatility in prices that occurred in 2004. A barrel of oil increased in price from $33 in January 2004 to a peak of $55 in October 04. It has fallen back to the $45 range recently. At the national level, every $10 increase in the price of oil represents the equivalent of about a $70 billion tax on consumers as expenditures on other goods and services are diverted to pay for higher energy costs.

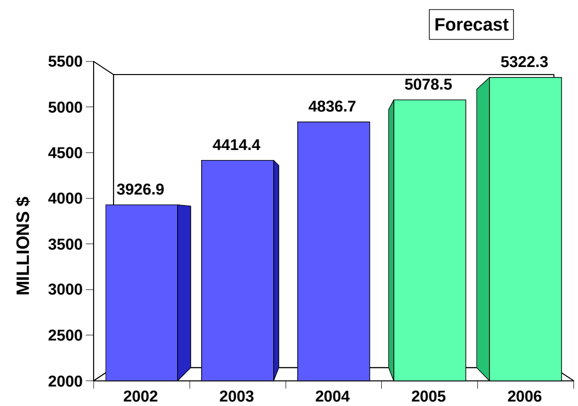
Final energy use makes up an estimated 7% of the Consumer Price Index in terms of its relative importance among all goods and services purchased by consumers. Medical care costs represent another 6%. The chart below provides a perspective on the change in the national costs of both final energy use and medical care compared to the increase in total personal income in New Jersey. From the first quarter of 2002 until the third quarter of 2004, total personal income in New Jersey increased by 7.2% as the state emerged from the national recession and began to recover jobs and economic activity. Energy costs, however, have increased by 33% over the same time while medical care costs have gone up by 11%. Because the demand for both energy and medical care is not very sensitive to price, particularly in the short run, these two components of consumer spending have diverted significant amounts of consumer spending from other goods and services. At the level of the national economy, this drag on consumer spending was responsible for the slowdown in the economy after the big oil price spike in the spring when the growth in consumer expenditures fell from a 4.1% pace in the first quarter to 1.6 % increase in the second quarter.

Indices: New Jersey Total Personal Income vs. CPI-Energy and CPI-Medical Care
1st Quarter 2002 - 3rd Quarter 2004
(2002.1 = 100.0)



Residential construction had another good year in 2004 supported by low mortgage rates and growth in incomes. Through the first ten months of 2004, permits are up 6% over 2003, and should approach 35,000 for the entire year. Home prices continue to soar. The price of an existing single-family home in New Jersey rose by 12%. The value of residential construction contracts increased by 9.6 % in 2004 as a result of the increase in housing activity and the continued trend toward larger homes. Constraints on the supply of building sites and the effects of rising mortgage rates will slow new building activity in 2005. The increase in the value of construction contracts should moderate to 5%.

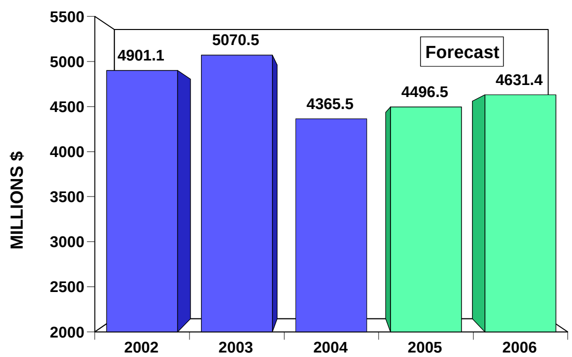
NJ Residential Construction Contracts, $



Non-residential construction in New Jersey continues to be affected by rising vacancy rates for commercial space. In the 3rd quarter of 2004, the vacancy rate for Class A space in the 10 county Northern and Central New Jersey was 27%, up from 21.6% in the second quarter. Despite strong job growth and the fact that the total number of jobs in New Jersey now exceeds the previous peak, about 12% less office space is being utilized as businesses have imposed more cost discipline. Non-residential construction contracts declined in 2004 (through November) by 14% from the comparable period in 2003.

There has been continued strength in education building as a result of the NJ school construction program and this has supported non-residential contracts. As job growth continues and the housing market cools, activity in non-residential construction should improve over the next several years.

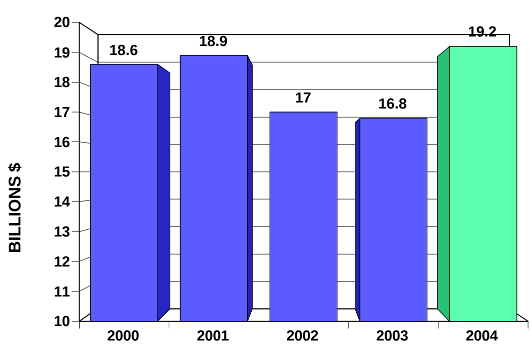
NJ Non-Residential Construction Contracts, $



International Trade

International trade was the surprise sector for the state in 2004. New Jersey's exports increased by a strong 14.7% (through the 3rd quarter) as the depreciation of the dollar began to significantly improve the competitiveness of U.S. goods and services. U.S. exports rose by 13.8% in the same period. The state's largest export destinations are Canada, the United Kingdom, Germany, Israel, Japan, and Mexico. Exports totaled $14.2 billion through the 3rd quarter and the major categories of exported goods were chemicals, computers and electronic products, transportation equipment, and machinery. In addition, the large increase in the volume of both exports and imports in the region's port areas benefited the transportation, logistics, and warehouse activity in New Jersey. With further declines in the dollar expected in 2005, exports should continue to support economic growth in the state.

New Jersey Exports, in $ Billions



The Region

The recovery of the region continued in 2004 with New York City finally adding jobs after several difficult years following the attacks of September 11th 2001. For 2004 (through November), employment increased by 31,100 jobs, still leaving the City 205,700 jobs below its December 2000 level. Nevertheless, 2004 was the first year since 2000 when jobs actually increased. The largest job gains occurred in professional services, hospitality, and retail trade. The weaker dollar has given tourism a significant boost and the number of foreign visitors to New York rose by a robust 10.2% in 2004, but is still about 22% below its 2000 level. Hotel occupancy, ridership on the subways, bridge and tunnel crossings, and port traffic are all up and commercial vacancy rates have fallen.

One important sector that has not added jobs is finance, the most visible and economically powerful part of the City's economy. Despite strong gains in the capital markets in the last two years, employment in the financial industry in New York City has essentially been flat since August 2003. Financial jobs were moved out of the City after the attacks of 9/11. In addition, technological innovations and outsourcing have eliminated and dispersed many lower paying financial sector jobs since then. This trend is likely to continue. The financial jobs that remain in the City are well paying and salary bonuses for the sector in 2004 are estimated at $15.9 billion. These bonuses will provide strong support for consumer and housing expenditures in the region.

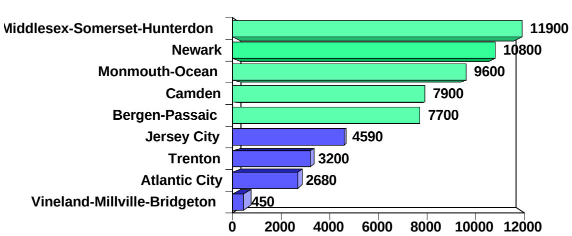
New Jersey has been the partial beneficiary of the dispersal of financial jobs from New York City. Since September 2001, employment in financial activities in New Jersey has increased by 21,700 and is now at an all-time high of nearly 288,000 jobs. Due to the destruction and disruption caused by the terrorist attacks in the immediate months after 9/11, New Jersey received over 14,000 jobs as New York firms relocated offices and people in order to continue operations. About 5,000 of these jobs returned to New York City in the first half of 2002, but job growth in the finance sector in New Jersey resumed by July 2002 and has increased steadily since. Further improvement in the overall New York City economy is anticipated in 2005 and this will support economic activity in the region.

Economic conditions in Philadelphia stabilized in 2004. Employment in the private sector increased by 1,700 jobs after falling by 4,500 jobs a year earlier. Last year, educational and health services added a strong 7,700 jobs, but jobs declined in manufacturing, trade, and finance. The outlook is for improving labor market conditions in Philadelphia with accompanying gains in income and consumer spending that will benefit the region.

New Jersey Labor Markets

The strong employment gains for the state in 2004 were reflected in all the state's labor market areas. The Middlesex-Somerset-Hunterdon labor market area added 11,900 jobs, the largest increase of all the state's labor market areas. The Monmouth-Ocean labor market was the fastest growing area (2.4%, or 9,600 jobs). Strong absolute gains also occurred in Newark (10,800 jobs), Camden (7,900 jobs), and Bergen-Passaic (7,700). New Jersey labor markets will be redefined in 2005 following changes based on commuting and population patterns from the U.S. Census of 2000.

New Jersey Labor Market Non-Ag Payroll Employment Change, 2003-04 (In Thousands)



Summary

Over the last six years, through good times and bad, New Jersey's economy has outperformed the national economy. We are likely to see that streak continue in 2005. However, it is vital that public policy ensure that New Jersey remains an attractive place for individuals and businesses to locate and invest.

NJ COUNCIL OF ECONOMIC ADVISORS

About the Council of Economic Advisors: Established by law in 1993 (P.L. 1993, Chapter 149).

The Council is an advisory organization reporting directly and independently to the Executive branch of government, the Legislature and the public.

The Council is charged with the preparation of an Annual Report and a mid-year Report analyzing current New Jersey economic conditions and forecasting future developments, assists the Executive in preparation of the annual budget message, and advises the Governor and Legislature on public policies impacting the State's economy.

The Council is comprised of a Chairman appointed by the Governor and legislative appointees.

<u>The Council members are</u>:
Dr. Joseph J. Seneca, Chairman
Members: Steven K. Brisgel, Victor H. Boyajian, Esq., C. Mark Dadd, Frederick Kelly, PhD., George Zoffinger

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New Jersey Economic Outlook & Review For 2005-06

(Current $ or Nos.)	2001	2002	2003	2004	NJCEA Forecast 2005	NJCEA Forecast 2006
Gross State Product (bill $)	362.9	380.2	397.5	416.6	435.7	454.5
Personal Income (bill $)[1]	332.7	337.9	345.6	363.5	380.6	393.9
Retail Sales (bill $)	105.0	106.7	109.4	114.3	119.0	122.8
New Vehicle Registrations (000)[2]	655.5	646.4	659.1	643.9	640.7	642.6
Non-Res. Construction Contracts (mill $)[3]	5,017.6	4,901.1	5,070.5	4,365.5	4,496.5	4,631.4
Residential Building Permits (No.)	28,277	30,450	34,584	35,000	34,000	32,000
Res. Construction Contracts (mill $)[4]	3,885.7	3,926.9	4,414.4	4,836.7	5,078.5	5,322.3
CPI (1982-1984=100)	187.1	191.9	197.8	204.8	211.4	217.2
(Real 1982$)						
Gross State Product (bill $)	193.9	198.1	200.9	203.4	206.1	209.2
Personal Income (bill $)	177.8	176.1	174.7	177.5	180.0	181.4
Retail Sales (bill $)	56.1	55.6	55.3	55.8	56.3	56.5
Employment[5]						
Total Nonfarm (000)	3,997.2	3,983.9	3,980.3	4,039.8	4,096.4	4,141.5
Manufacturing (000)	401.2	367.5	351.7	345.6	345.6	345.6
Private Service-Providing (000)	2,832.8	2,838.8	2,843.4	2,888.1	2,943.0	2,990.1
Government (000)	602.6	613.5	624.3	640.9	650.5	660.3
Unemployment Rate (%)	4.2	5.8	5.9	4.9	4.6	4.4

Percentage Change from previous year:	2002	2003	2004	2005	2006
(Current $ or Nos.)					
Gross State Product	4.8	4.6	4.8	4.6	4.3
Personal Income[1]	1.5	2.3	5.2	4.7	3.5
Retail Sales	1.6	2.5	4.5	4.1	3.2
New Vehicle Registrations	-1.4	2.0	-2.3	-0.5	0.3
Non-Res. Construction Contracts	-2.3	3.5	-13.9	3.0	3.0
Residential Building Permits	7.7	13.6	1.2	-2.9	-5.9
Res. Construction Contracts	1.1	12.4	9.6	5.0	4.8
CPI (1982-1984=100)	2.6	3.1	3.5	3.2	2.7
(Real 1982$)					
Gross State Product	2.1	1.4	1.2	1.3	1.5
Personal Income	-1.0	-0.8	1.6	1.4	0.7
Retail Sales	-0.9	-0.5	0.9	0.9	0.4
Employment					
Total Nonfarm	-0.3	-0.1	1.5	1.4	1.1
Manufacturing	-8.4	-4.3	-1.7	0.0	0.0
Private Service-Providing	0.2	0.2	1.6	1.9	1.6
Government	1.8	1.8	2.7	1.5	1.5

1. The estimated 5.2% increase in personal Income for 2004 is based on the increase of the average of the first three quarters of 2004 over the first three quarters of 2003.
2. The 2004 total for New Vehicle Registrations was computed as the sum of registrations reported for the months January-November, plus a December estimate calculated as the average of the January through November totals.
3. The 2004 total value for Non-Residential Construction Contracts was computed as the sum of the totals reported for the months January-November, plus a December estimate calculated as the average of the January through November totals.
4. The 2004 total value for Residential Construction Contracts was computed as the sum of the totals reported for the months January-November, plus a December estimate calculated as the average of the January through November totals.
5. Employment figures for 2001-2004 are based on non-seasonally adjusted 12-month averages.

OFFICE OF LEGISLATIVE SERVICES

The Office of Legislative Services provides nonpartisan assistance to the State Legislature in the areas of legal, fiscal, research, bill drafting, committee staffing and administrative services. It operates under the jurisdiction of the Legislative Services Commission, a bipartisan body consisting of eight members of each House. The Executive Director supervises and directs the Office of Legislative Services.

The Legislative Budget and Finance Officer is the chief fiscal officer for the Legislature. The Legislative Budget and Finance Officer collects and presents fiscal information for the Legislature; serves as Secretary to the Joint Budget Oversight Committee; attends upon the Appropriations Committees during review of the Governor's Budget recommendations; reports on such matters as the committees or Legislature may direct; administers the fiscal note process and has statutory responsibilities for the review of appropriations transfers and other State fiscal transactions.

The Office of Legislative Services Central Staff provides a variety of legal, fiscal, research and administrative services to individual legislators, legislative officers, legislative committees and commissions, and partisan staff. The central staff is organized under the Central Staff Management Unit into ten subject area sections. Each section, under a section chief, includes legal, fiscal, and research staff for the standing reference committees of the Legislature and, upon request, to special commissions created by the Legislature. The central staff assists the Legislative Budget and Finance Officer in providing services to the Appropriations Committees during the budget review process.

Individuals wishing information and committee schedules on the FY 2006 budget are encouraged to contact:

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