Testimony of Acting State Treasurer
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Madam Chair. Distinguished members of the Senate Budget and Appropriations Committee.

Good afternoon.

With me today are Charlene Holzbaur, the Director of the Office of Management and Budget and Robert Peden, the Deputy Director of OMB.

The budget presented by Governor Corzine for FY 2009 is both fundamentally sound, and a fundamental change from budgets of the recent past.

It is fundamentally sound because it closely balances available recurring revenues with actual spending.

It is fundamentally different because it strikes this balance without relying on increased taxes, short-term fixes, non-recurring revenues, and one-time actions.

It is also fundamentally different because it reduces spending for only the fourth time in the last fifty years and represents the second largest decease in spending during that period of time

This budget is $500 million less than the one signed into law last June. Actual reductions, however, total $2.7 billion in order to offset mandatory cost pressures that would have otherwise brought spending to $35.7 billion.

As someone who has staffed budget committees, and as someone who has worked on State budgets with the executive branch for the better part of this decade, I can say in all candor that this budget is one of the most challenging I have ever been associated with.

Spending needs have never been more acute; from billions of dollars for required contributions to pensions and health care ...to billions more for property tax relief, and hospital funding...and a parade of spending priorities wanting for support.

The appetite for spending is simply ferocious.

At the same time, revenues have rarely been so limited. Revenues in FY 2009 are projected to increase by no more than $500 million.

This opening day hearing comes at a time when the nation is at the doorstep of a recession. Some analysts say we may have already crossed the threshold.

As such, the income to the State budget is not growing at a pace anywhere close to what is needed to support baked-in expenses. As well, raising more revenues through taxes in the current climate is economically perilous.

Equally important, the people who foot the bill are in no mood to sign a blank check to a government that assures them: we'll fix the problem; just trust us.

They've seen the problem develop and worsen over time. Spending obligations were incurred, with little thought to the consequences of not having a sustainable revenue source to pay for them. Rather than cut spending, the State found increasingly inventive ways to patch the revenue holes in the budget -- from borrowing and fund raids to one-shots and deferrals of obligations.

In short, when the state could have used a discipline for austerity, it had a mindset of prosperity.

As Governor Corzine will attest from his personal experiences at many town hall meetings around the state, the taxpaying public is sending an unmistakable message: Cut out the gimmicks; Cut government spending, and cut spending on government.

The Governor's budget for FY 2009 does all of these things.

It includes over $2.7 billion in actions to reduce spending, and decreases total expenditures by $500 million from the budget enacted last June.

It reduces the reliance on non-recurring resources from $1.8 billion to less than $600 million.

It reduces the size and the cost of government by over $350 million; Every State department is cut; there will be 3,000 fewer employees on the payroll by the end of next fiscal year.

At the same time, the proposed budget:

Maintains our commitment to property tax relief for the middle class;

Protects programs that provide public safety;

Protects programs that serve the needs of the most vulnerable;

Does not rely on any new or increased taxes; and

Distributes reductions in a fair and common sense manner.

Now, if you are a stakeholder at the receiving end of a budget item that's been eliminated or reduced, it is understandable for someone to object on the grounds of fairness.

This budget is replete with programs and services worthy of funding support.

Unfortunately, the budget is also shackled by mandatory expenses, such as pension and health care costs and debt service. These costs are growing and are crowding out New Jersey's ability to fund other meaningful priorities.

Spending pressures based solely on a continuation of existing policies would have grown the budget from the $33.5 billion in the current year to an estimated $35.7 billion in FY 2009. This growth was based on contractual, mandatory and statutory increases including over $500 million in additional costs for the new school funding formula.

As we looked to balance this budget, we recognized a fatal disconnect: only $32.5 billion in base revenues would be available to support $35.7 billion in spending – a $3.2 billion shortfall.

We closed the structural gap with $2.7 billion in actions that impact spending and the use of $500 million of the $834 million of excess surplus. This will be the last year that excess surplus will be used to fund recurring expenses.

Nearly $1.7 billion or over 60 percent of the spending actions are actual reductions to the base budget.

The other $1 billion represents reductions or limitations of growth and other actions to offset spending.

This $1 billion in growth limitations was not simply eliminating department wish lists.

I do not believe that any of us would call trying to provide a COLA for community providers a wish list item.

I also do not think any of us would call inflationary increases for municipalities, colleges and NJ Transit wish list items.

And finally, I do not think any of us would call increasing pension funding a wish list item.

Since 75 percent of State spending goes right back to New Jersey communities and citizens in the form of grants and aid, it is mathematically impossible to spare this portion of the budget from reductions in both base spending and growth.

We sought to minimize this impact by slicing heavily into the operations portion of our budget, which represents less than 20 percent of total spending.

The budget will reduce the size and cost of State government by over $350 million and the number of employees by approximately 3,000 through a combination of Early Retirement, attrition and targeted layoffs. This additional reduction of employees is on top of the 2,000 employees that have been eliminated since Governor Corzine took office.

The budget calls for the elimination of three Cabinet level agencies – the Departments of Agriculture and Personnel and the Commerce Commission. The essential functions of these agencies will be consolidated into other executive branch departments or agencies. The reductions to the executive branch are deeply rooted in the Governor's pronouncement that government will not only have to do more with less; government will undoubtedly have to do less.

I truly believe that during the next year as Departments are faced with the realization that they will have approximately 3,000 fewer employees that there will be a significant change in what State government does and does not do in the future. As Departments grapple with this we certainly will be coming back to the Legislature to eliminate statutory mandates on the departments that simply should no longer be a priority.

I noted earlier that growing obligations were crowding out other, more meaningful spending needs. By making cuts which rightsize our expenses with revenues, the net effect will be to allow us to preserve funding for core priorities.

Accordingly, our reductions make it possible to increase recurring property tax relief by $73 million from the amount spent in the current year. This budget will provide nearly $16.7 billion in total property tax relief which still represents more than 50 percent of the budget.

The majority of the funding for property tax relief represents the $11.5 billion in support of public education which is $600 million above the current year appropriation. State aid for education represents over one-third of the total budget.

Notwithstanding fiscal pressures, this budget allocates $2.5 billion for direct property tax relief to homeowners.

This funding ensures that 1.6 million homeowners will continue to receive average rebates of approximately $1,000.

In all, 90 percent of homeowners will continue to receive rebates while 1.2 million homeowners, or the 70 percent with incomes below $100,000, will receive the same rebate amount.

Protecting the rebates for families below $100,000 is a key component of this budget since that group of families faces the most pressure from the regressive property tax.

Due to fiscal constraints, the budget will also include a reduction in municipal aid. The budget will provide over $1.8 billion in aid to municipalities, a decrease of approximately $190 million.

Rather than simply reducing aid to all municipalities across the board, this budget would target a portion of the reduction. Under this budget proposal, communities with populations below 5,000 would see their CMPTRA aid eliminated, while towns between

5,000 and 10,000 would see their CMPTRA reduced by 50 percent. There are no cuts to the other mainstay resource for all municipalities – the Energy Receipts program.

Let me be clear, the municipalities with populations of less than 5,000 are not losing all of their aid.

In fact, in the current year, this group of municipalities received $85 million while under this proposal they would still receive $50 million.

The municipalities with population between 5,000 and 10,000 will receive a reduction of aid from $164 million to $135 million. The bulk of the $170 million reduction in formula based aid will come from the municipalities with more than 10,000 people.

We understand that this reduction is difficult to absorb. We also understand that some small towns are already working efficiently and finding ways to share and regionalize services. We applaud such efforts, with the caveat that more must be done to lower the cost of government.

This group of towns will be given priority standing in the awarding of the $32 million in grants from state funds that encourage consolidation and shared services.

We have heard the concerns regarding the abruptness of this reduction in aid to the municipalities under 5,000. The Administration has already stated that we are willing to consider some type of phase in;

however, this must be achieved in the overall context of a $33 billion spending plan. If spending for municipal aid goes up then spending elsewhere in the budget has to go down.

We also know that, on average, 55 percent of the local tax bill pays for local education costs. The share grows to about three-quarters for many of New Jersey's suburban municipalities.

Therefore local taxpayers will see considerable relief in their tax bill from the additional funding we're investing through the new school funding formula.

As we struggled with finding $2.7 billion in savings to balance this budget we made the determination to attempt to treat the major spending areas of this budget in a fair and consistent manner.

Our goal was to protect the programs that support the most vulnerable and the social safety net as well as programs that impact the middle class.

As previously discussed, we are proposing a 10 percent reduction in municipal aid.

Likewise, we are proposing to reduce operating support to the states colleges and universities by 10 percent as well.

The budget will still provide overall support for higher education of $2.1 billion, which represents an overall reduction of $76 million from FY 2008, or only 3.5 percent.

Another significant area of reduction is the State's support of hospitals. This budget will provide $900 million in various aid to hospitals which represents a reduction of $144 million.

More specifically, the budget will provide $608 million for the Charity Care program, a reduction of $108 million from the current level.

A portion of the $608 million will not be allocated through the formula but instead will be held in a newly created Health Care Stabilization Fund to assist hospitals and other health care facilities facing specific financial needs during the fiscal year.

As with municipal aid, we made the decision not to simply implement this reduction in an across-the-board manner.

Instead we have proposed a new distribution that is not only based on updated information but also provides the majority of the aid to those hospitals that provide the majority of the care.

There are other significant areas impacted by this budget that if we do not discuss today, they will be central focus of the upcoming hearings with each of our departments.

We understand that just as the $190 million reduction has an impact on municipalities, the $6 million reduction will have an impact on the arts; the proposed savings in prescription drug programs will have an impact on Medicaid and PAAD clients, pharmacists and drug manufacturers.

However, we all must understand in order to balance a budget with at most $32.5 billion in revenue that programs we have been supporting for the past decade are simply no longer affordable.

We've addressed the appropriations portion of the budget. Now I would like to walk through the revenue side.

First, as we moved closer to presenting a budget at the end of February, we saw signs that the economy was beginning to impact our current year revenue collections and our forecast for FY 2009 revenues. Sensing the trend, our overall revenues we reduced by $500 million and thus our spending was also reduced by an additional $500 million.

As a result, the overall increase in revenues for FY 2009 is projected to be under $500 million, which is less than the increase in school funding provided in this budget.

As you have heard earlier today from David Rosen, our cautious approach was warranted.

As with the first two budgets of this Administration, the overall difference between OLS and the Administration is negligible. A net difference of $133 million in revenue from a base of over $64 billion is only two-tenths of one percent.

I believe it is possible that we may even be closer after the April collections are counted and we have another quarter of economic data to consider. The bigger concern I have is how the changing economic forecast will impact our projections for FY 2009.

Both OLS and I agree that there is of a risk that further downward revisions may have to be made to the revenue projections as we move forward. Considering that we have only a $600 million surplus in a $33 billion budget, there is no margin for error because we simply must maintain a real surplus of at least $600 million.

For the current year, we have revised downward our forecast for the Gross Income Tax by $200 million. This revision reflects expected modest growth for calendar year 2007, but weaker than anticipated economic conditions for calendar 2008.

I would like to repeat here that the downward revision is tied to weaker economic conditions and not to any trends suggesting that New Jersey is losing high income earners. As you know, approximately 40 percent of our income taxes are paid by the top one percent of income earners. Although some studies suggest that New Jersey is seeing an outmigration of these taxpayers, statistics strongly belie this premise.

For example, about 39 thousand income tax returns were filed in 2003 by taxpayers earning more than $500,000. In 2006, that population has swelled to approximately 63 thousand filers.

We anticipate the Sales Tax to end the year closely in line with original estimates.

The Corporation Business Tax is expected to end the current year at $2.7 billion, or $155 million above projections. We remain concerned, however, over how underlying economic conditions will impact our CBT in FY 2009.

For FY 2009, we project GIT collections to grow by a modest $694 million over the current year. A basic, underlying growth rate of 5.7 percent reflects weakening income growth trends and a softer financial market.

The forecast of $ 8.7 billion in Sales Tax revenue for FY 2009 is an increase of $220 million, or 2.6 percent. This rate reflects the forecast for soft economic conditions moving forward.

And for FY 2009, we are forecasting a reduction in collections from the Corporation Business Tax....from $2.7 billion to $2.5 billion next year. This net reduction is the result of the expiration of the AMA, AMA credits and the growth in the net operating loss deductibility.

The proposed $33 billion budget delivers on the first component of the Governor's four-pronged strategy to restructure state finances.

This budget not only achieves the Governor's goal of freezing spending for the current year – it actually reduces spending.

It also moves us closer to the structural balance of having recurring revenues equal recurring spending. Next year we will achieve structural balance.

However, even after $2.7 billion savings initiatives in the proposed budget, we are still projecting a structural gap of nearly $2 billion in FY 2010 simply based on projections of current revenues and mandatory spending increases.

Recognition of this gap is a signal that we should not revert to past practices in finalizing a budget this year. Any use of added non-recurring revenues or other actions that defer the problem to the next year will simply increase the gap for FY 2010. We must avoid this trap or else the cycle of deficit budgeting will only continue.

The ability to pay down the State's debt and reduce the annual debt service is vitally important to limiting future spending increases while at the same time maintaining programs and services.

We're spending close to $100 million more in the next budget on debt service than we are spending in the current year. This is one of the few areas in this budget that is increasing. The amount spent on debt service will continue to grow in future years.

A reduction in the State's debt would result in a debt service savings of anywhere from $500 million to $1 billion, which would be a significant portion of the projected deficit for FY 2010. The reduction in debt service is an action that has no impact on any State service or program. Absent a reduction in an area such as debt service, the State will continually need to reduce base spending by hundreds of millions of dollars to offset mandatory and contractual increases.

Given the public's aversion to tax increases, and the unpopularity of spending reductions, we are between the proverbial rock and a hard place. The Corzine administration prefers to call this a turning point and looks forward to working in partnership with you to reset State finances.

At this time, I would welcome any questions from the committee.