STOCKTON UNIVERSITY

stockton.edu
New Jersey's Distinctive Public University

Stockton's Hughes Center Offers Ways to Improve N.J. Revenue Forecasts, Reduce Budget 'Surprises'

For Immediate Release

Monday, February 06, 2017

Contact: **Maryjane Briant**
News and Media Relations Director
Galloway, N.J. 08205
Maryjane.Briant@stockton.edu
(609) 652-4593
stockton.edu/media

Galloway, N.J. - New Jersey's system of revenue forecasting has repeatedly led to budget difficulties, including a shortfall of nearly $1 billion in 2014. Research published today by the William J. Hughes Center for Public Policy at Stockton University reveals key findings about the state's process and outlines opportunities to improve it through "building a shared reality" between the governor and the Legislature.

"State Revenue Forecasts: Building a Shared Reality" compares New Jersey's revenue forecasting with that of neighboring Delaware, Pennsylvania and New York from 2002-2015. In contrast to those states, only New Jersey's revenues have failed to recover to pre-recession peaks, the study found.

"We find the biggest shortcoming to be in the state's failure to establish and maintain a Surplus Revenue Fund sufficient to manage forecasting errors," said authors Daniel Mallinson and David Carr, both professors in Stockton University's Political Science program. Carr also serves as director of Research and Policy Analysis at the Hughes Center.

Other key findings include:

- Deposits into the Surplus Revenue Fund, for the purpose of protecting against revenue volatility, are dependent on a year-end surplus between forecasted and actual revenues. This less than proactive approach is uncomfortably similar to explanations of why most Americans have not saved enough for retirement.

- The revenue stream feeding the Surplus Revenue Fund is heavily reliant on sales tax revenue which, according to the Treasurer's Tax Expenditures Report, is reduced significantly by exemptions and exclusions. (A Hughes Center study by Mallinson and Carr released in January showed that a partial estimate of the cost of New

-more-

-continued from page 1-

Jersey's many tax breaks totals at least $23.5 billion for fiscal year 2017, a figure that equals roughly two-thirds of the state's annual budget of $34.8 billion.)

- Since 2009 the Surplus Revenue Fund has been virtually empty.
- In 2015, New Jersey only had enough reserve funds (Surplus Revenue Fund plus end of year balances) to operate government for 9.2 days.
- Since 2010 New Jersey has regularly overestimated revenues resulting in several "April Surprises" which, coming so close to the end of the fiscal year have required short term fixes which have contributed to the State's declining bond ratings.
- Although differences between forecasted and actual revenues in New Jersey are small in percentage terms, in absolute dollars they run in the millions and occasionally, billions of dollars. Consequently, they have significant programmatic and political consequences.
- Even as New Jersey has suffered a succession of "April Surprises," to our knowledge, it has not undertaken any systematic initiative to improve its approach to revenue forecasting. Both legislative and executive branch agencies appear to lack the staff and resources to do so. While all revenue forecasts have error, even a small decrease in forecasting error might be significant in absolute dollars.
- New Jersey maintains a competing, rather than a consensus forecasting model with the executive branch and the legislative branch offering competing forecasts.
- The literature on revenue forecasting suggests that consensus forecasting does not produce more accurate forecasts. Its principal advantage is political. It creates a shared reality as the budget process unfolds following the governor's budget address and often introduces greater transparency into revenue forecasting processes.
- Compared to both New York and Delaware, information on New Jersey's revenue forecasting methodologies and results is much less available and transparent.

The state's proposal for fiscal year 2018, which begins July 1, will be outlined by Gov. Chris Christie in his last gubernatorial budget address on Feb. 28.

The study outlines opportunities to improve revenue forecasting, including:

- **Building N.J. reserve funds up front**
  Making deposits into the fund as a regular practice. This might be done by setting aside a percentage of the surplus general revenue funds or by limiting the amount of forecasted revenues that can be appropriated and spent, depositing the remaining funds up front.

- **Establishing Surplus Revenue Fund targets** to reflect historical and projected patterns in forecasting accuracy.

-more-

-continued from page 2-

- **Using Consensus Forecasting**
  Instead of producing competing revenue forecasts, the governor and the Legislature should work together. "Consensus forecasting brings a critical advantage to the table: a shared reality and a shared vision of the economic parameters of the state's fiscal future," the authors said.

- **Including Longer Term Forecasts in the Process**
  In contrast with the other states studied in this report, New Jersey stands out in its short-term perspective for revenue forecasting. ... Without long-term forecasts there is no benchmark for determining the long-term impacts of current legislative initiatives. Nor is there a basis for longer term financial planning. This merely induces a tendency to the short-term "fixes" that New Jersey has used so frequently.

- **Regularly Analyzing and Monitoring Sources of Revenue Volatility & Forecasting Error**
  The state should be conducting or sponsoring research on the sources of revenue volatility, as well as evaluating the effectiveness of its forecasting methodologies.

- **Updating Forecasts Throughout the Year**
  New Jersey's last revenue forecast takes place more than a year in advance of the end of the fiscal year being planned. In contrast, Delaware and New York update forecasts six times a year.

  At a minimum, New Jersey should identify the conditions that might require a mid-year update to the revenue forecast.

- **Making the Forecasting Process More Transparent and Accessible**
  The Department of the Treasury and the Office of Legislative Services issue updated revenue forecasts, but these are compared to the revenues certified by the governor at the time the Appropriations Act is passed, which may be woefully out of date with regard to the state's economic conditions.

  Most citizens would have to actively look for them. It would also help if these forecast updates used the same methodology, and ideally, if they came up with a single number. Regular updates would provide opportunities to make appropriate adjustments earlier in the year.

The complete study is found at stockton.edu/hughescenter.
To arrange interviews with Mallinson or Carr, contact Maryjane Briant at 609-652-4593; or maryjane.briant@stockton.edu

About the Hughes Center

The William J. Hughes Center for Public Policy (www.stockton.edu/hughescenter) at Stockton University serves as a catalyst for research, analysis and innovative policy solutions on the economic, social and cultural issues facing New Jersey, and promotes the civic life of New Jersey through engagement, education and research. The center is named for William J. Hughes, whose distinguished career includes service in the U.S. House of Representatives, Ambassador to Panama and as a Distinguished Visiting Professor at Stockton. The Hughes Center can be found at https://www.facebook.com/StocktonHughesCenter and can be followed on Twitter @hughescenter.

# # #