New Jersey's Fiscal Future

New Jersey's Multi-Year Structural Deficit: Current Services Budget Projections, Economic Uncertainty, and the Looming Fiscal Cliff

By the Multi-Year Budget Workgroup

Rowan University
STEVE SWEENEY CENTER
FOR PUBLIC POLICY

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Preface: About the Multi-Year Budget Workgroup

Three years ago, the Sweeney Center for Public Policy at Rowan University convened the Multi-Year Budget Workgroup (MYBW), a bipartisan team of former high-ranking administration and legislative budget officials, policy experts, economists and academics, to provide independent analysis of the long-term budget problems facing New Jersey.

New Jersey had consistently graded low on the Volcker Alliance's State Budget Report Cards primarily because of its failure to implement multi-year budgeting and consensus revenue forecasting. The Multi Year Budget Workgroup was created to provide that analysis, which is performed in most states by government officials or quasi-government agencies.

This report marks the fourth budget year that the MYBW has provided an independent multi-year economic and revenue forecast, calculated the cost of maintaining state aid and programs at current service levels and funding new programs required by law, and showed the gap between projected revenues and expenditures.

The MYBW was modeled after the blue-ribbon *Facing Our Future* panel put together by the Council of New Jersey Grantmakers in 2010 to develop multi-year revenue projections and analyze whether those revenues would be sufficient to cover the cost of maintaining state services at current levels for the next five years. Richard Keevey and Ray Caprio, who developed the projections for *Facing Our Future*, both serve on our workgroup.

To avoid conflicts of interest, the MYBW does not include any current state officials or candidates for state office. Former Senate President Steve Sweeney withdrew from participation in the workgroup 14 months ago after declaring his candidacy for governor.

Dr. Charles Steindel, who developed economic forecasts for the Federal Reserve Bank of New York and the New Jersey Treasury Department, serves as our chief economist. His forecasts are the starting point for our multi-year budget analyses, which are developed by consensus. As fiscal policy practitioners serving in multiple roles with different perspectives, we can reach agreement on the numbers and the challenges but reserve the right to disagree on the solutions.

The MYBW will continue to provide economic forecasts and multi-year revenue and expenditure projections to the Governor and the Legislature in February and June each year.

Like our earlier reports, this analysis seeks to provide insights and inform the public debate on the fiscal policy challenges that New Jersey faces as the Administration and legislative leaders prepare the FY26 state budget.

Executive Summary

For the past three fiscal years, the New Jersey state government has run significant structural deficits, spending $1.8 billion, $3.2 billion and $2.1 billion more than it received or expected to receive in revenues.

These "red ink" budgets were covered largely by drawing down the record $10.7 billion surplus built up at the end of FY2022 by the infusion of billions of dollars in federal aid that flowed in during the Covid-19 crisis and by tapping into the Debt Defeasance Fund created after the state took out a $4.3 billion Covid-19 emergency loan from the federal government.

Those fiscal maneuvers reduced the state's projected budget surplus to $6.197 billion in the current FY2025 budget year that ends June 30 – a 10.9% surplus that is healthy by historic standards compared to past administrations whose surpluses usually often ran closer to 1% to 2% of state revenues, but at the low end of the 24% national average currently maintained by state governments. Only seven states have a lower surplus balance as a percentage of revenue.

The Multi-Year Budget Workgroup projects that New Jersey will continue to face structural budget gaps over the next four years, as revenues are projected to fall an average of at least $2.2 billion short of the amount needed to maintain state aid and programs at current service levels, fund new programs established by law and maintain an adequate surplus.

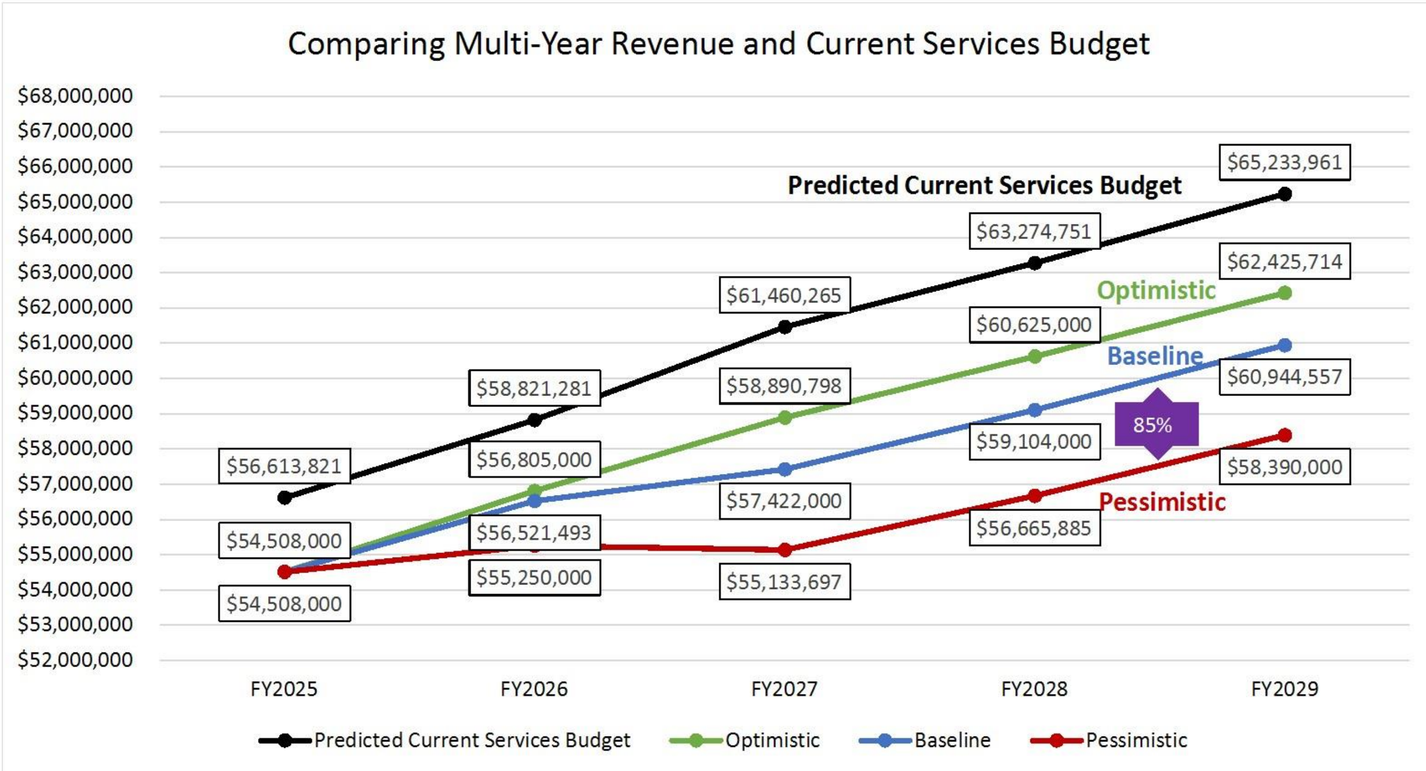
That $2.2 billion average gap is an optimistic scenario.

Based on our economic forecast, revenue projections and Current Services Budget analysis, the Multi-Year Budget Workgroup projects that there is an 85% likelihood that state revenues will fall an average of $3.7 billion to $6.7 billion short of the amount needed to maintain state aid and programs at current service levels each budget year from FY2026 to FY2029, spanning most of the four-year term of the new governor who will be elected in November.

The New Jersey State Constitution requires the Governor and Legislature to enact a balanced budget by June 30 each year, so each year's structural gap would have to be covered in the annual budget by spending cuts, revenue increases and diversions from the surplus for as long as it is deemed prudent.

Balancing this year's budget required the state to pull $2.48 billion from the surplus, transfer $585 million from the Debt Defeasance Fund, and divert $1.023 billion from the retroactive restoration of the Corporate Business Tax surcharge on companies earning more than $10 million a year in profits in New Jersey that is supposed to be used as a dedicated source of funding for New Jersey Transit starting in FY2026.

The Murphy Administration set expectations for its upcoming Budget Address by projecting in background discussions with reporters that it will need to cover a $3.7 billion structural gap in this year's budget. As a first step, the state Office of Management and Budget last October directed state agencies to prepare their budgets for FY2026 with 5% spending cut



contingency plans; the Governor's Office followed up in November with a partial freeze on pay raises and new hires.

Complicating the FY2026 budget task for the Governor and Legislature is the extraordinary level of volatility in economic forecasts and corresponding revenue projections caused by the uncertainty over the impact of Trump Administration policies on tariffs, deportations of immigrant workers, inflation and interest rates.

In addition, cuts in Medicaid, education aid to states and cities, higher education research grants, federal grants to nonprofit providers of social services, and the federal workforce being contemplated by the Trump Administration and Congress could add hundreds of millions of dollars to the structural deficit as the Governor and Legislature weigh the need to increase state funding to make up for federal cuts.

Complicating the political calculus on the budget is the fact that all 80 seats in the New Jersey Assembly are up for election this year and that both parties will be selecting their gubernatorial nominees in the June 10 primary as the Governor and Legislature head into the final weeks of budget negotiations.

As in our previous 2022, 2023 and 2024 multi-year budget reports , the Multi-Year Budget Workgroup's calculations of the gap between projected revenues and future expenditure needs are based on the methodology developed in 2021 by former Senate Minority Leader Steve Oroho (R-Sussex) and Senate Budget Committee Chair Paul Sarlo (D-Bergen) in Senate Bill 654, the bill that bipartisan would have required the Governor and Legislature to implement consensus revenue forecasting with five-year revenue forecasts and expenditure projections using a Current Services Budget model.

The Multi-Year Budget Workgroup's Current Services Budget projects state spending to increase from $56.613 billion in the current FY24 budget to $65.256 billion in FY29. That four-year projected budget increase averages 3.8% a year. That compares to a 7.9% average annual increase for the eight years from Republican Gov. Christie's last $34.670 billion budget in FY2018 through Gov. Murphy's seventh budget in FY2025.

The Current Services Budget for FY2026 through FY2029 includes the projected full cost of the StayNJ, ANCHOR and Senior Freeze property tax relief programs, including a $900 million jump for StayNJ in FY2027 when the full-year program is to be enacted, and a $767 million increase for NJ Transit in FY2026 rising to $914 million in FY2029 to cover deficits left over when the last of the federal Covid-19-related operating assistance ran out in FY2025.

Relatively flat funding for pensions and debt service is offset by a projected 5.1% increase in state healthcare costs and in health benefits costs for current state workers and both teacher and state worker retirees based on federal Centers for Medicare and Medicaid Services projections. Other spending is calculated to rise 3% annually in accordance with the standard followed by the Oroho-Sarlo bill.

The Current Services Budget does not include the $600 million in one-shot targeted budget add-ons for specific municipalities, school districts, colleges, non-profit organizations and community programs in the FY25 budget as base spending for the purpose of calculating future budgets because the "Christmas tree" list changes from year to year and is among the first cuts in years of fiscal crisis.

As in previous years, the Multi-Year Budget Workgroup developed three sets of revenue projections: Baseline (45% likely), Pessimistic (40% likely) and Optimistic (15% likely) and matched those forecasts with the Current Services Budget projections for each year.

- Under the Baseline scenario, revenues for FY26 to FY29 would result in a cumulative $14.78 billion shortfall in total collections needed to cover projected Current Services Budget costs.

Five-Year Gap Between Current Services NJ State Budget and Revenue Projections

For three fiscal years, from FY23 to to the upcoming budget proposed for FY25, New Jersey state government will be running a structural deficit, with state spending exceeding projected revenues by $1.8 billion or more annually. To cover those gaps, the state plans to spend down the record $10.7 billion surplus built with federal aid during the Covid-19 pandemic to $6.3 billion, and is proposing a $1.023 billion Corporation Business Tax hike to reduce this year's deficit and cover NJ Transit's upcoming fiscal cliff. Even with passage of the CBT hike or another revenue-raiser similar in size, the Multi-Year Budget Workgroup projects that the state will face continuing structural deficits between expected revenues and the amount needed to maintain current service and state aid levels, fund newly enacted programs and maintain an acceptable surplus from FY26 to FY28. Under the MYBW's three revenue scenarios, the annual structural gap is projected to range from an average of $2.2 billion per year under the Optimistic scenario to a $5.7 billion average under the Pessimistic scenario. The New Jersey Constitution requires a passage of a balanced budget by June 30 each year.

	FY2022	FY2023	FY2024	FY2025	FY2026	FY2027	FY2028
Projected Current Services Budget	$48,787,000	$54,642,000	$55,501,000	$56,052,000	$59,013,206	$61,135,447	$63,008,689
Treasury Revenue Projections	$53,052,000	$52,840,000	$52,304,000	$54,249,000			
Treasury Projected Closing Surplus	$10,736,000	$9,986,704	$8,180,172	$6,300,000			
Debt Defeasance Fund Surplus			$1,200,000	$600,000			
Baseline							
Projected Revenue			$52,304,000	$54,249,000	$55,693,000	$57,589,000	$59,539,000
Structural deficit between projected revenue and projected spending			($3,197,000)	($1,803,000)	($3,320,206)	($3,546,447)	($3,469,689)
Surpluses tapped to cover structural deficit			$1,806,532	$2,480,172			
Budget differential if remaining surplus is applied to cover gap					$2,979,794	($566,653)	($4,036,342)
Pessimistic							
Projected Revenue			$52,304,000	$54,249,000	$53,885,000	$55,212,000	$56,727,000
Structural deficit between projected revenue and projected spending			($3,197,000)	($1,803,000)	($5,128,206)	($5,923,447)	($6,281,689)
Surpluses tapped to cover structural deficit			$1,806,532	$2,480,172			
Budget differential if remaining surplus is applied to cover gap					$1,171,794	($4,751,653)	($11,033,342)
Optimistic							
Projected Revenue			$52,304,000	$54,249,000	$56,658,000	$58,736,000	$61,021,000
Structural deficit between projected revenue and projected spending			($3,197,000)	($1,803,000)	($2,355,206)	($2,399,447)	($1,987,689)
Surpluses tapped to cover structural deficit			$1,806,532	$2,480,172			
Budget differential if remaining surplus is applied to cover gap					$3,944,794	$1,545,347	($442,342)

- Under the Pessimistic scenario, revenues for FY25 to FY29 would be a cumulative $26.76 billion below the revenue needed to continue to fund state services and state aid at Current Services Budget levels.
- Under the Optimistic scenario, revenue collections from FY26 to FY29 would be $8.79 billion short of the revenues needed to cover the full cost of the Current Services Budget.

Decisions made by the Governor and Legislature each year during the budget process will impact the size of these future cumulative shortfalls, as do mid-year decisions by the Administration such as hiring freezes and spending lapses.

However, the magnitude of the projected shortfalls is daunting, and significant cuts would be politically difficult, given that the lion's share of the $56.613 billion budget is "pass through" spending. This includes $21 billion in state aid to school districts and $18 billion in grants including the ANCHOR, Senior Freeze and new StayNJ property tax relief programs, the Medicaid-funded NJ FamilyCare program, community programs for the mentally ill and intellectually/ developmentally disabled, and aid to state universities, colleges and community colleges.

Another $7 billion goes to pension payments, $4 billion to employee and retiree health benefits, and $4 billion to debt service, leaving only $4.9 billion in the executive branch's operational budget – and much of that goes to staffing and operational costs for the state's prisons, psychiatric hospitals, developmental centers and veterans homes.

While the state is projected to finish FY25 with a $6.2 billion surplus, that cushion amounts to 10.9% of the budget. The StayNJ property tax relief program for seniors requires the maintenance of a 12% surplus, full funding of the state's school aid formula and a continuation of full pension payments as a condition for implementation of the program. Even without that requirement, a significant surplus would need to be retained from year to year to satisfy Wall Street bond rating agencies, which have upgraded New Jersey's credit rating in recent years due mainly to its healthy surpluses and completed ramp-up to full actuarially required pension payments.

New Jersey Economic Outlook

New Jersey's labor market softened in 2024. Job gains have ebbed, and the unemployment rate has stayed high. However, state output and income growth have been sustained at reasonable rates, and the housing market has remained robust.

According to preliminary data, New Jersey gained 30,300 jobs over the year ending in December 2024. That increase was well under 1%, and unemployment insurance records suggest there is likely to be a downward revision when the new benchmark figures are released in March. A marked increase in the education and health services sector more than accounted for all of the state's growth; the lion's share of other sectors was down over the year.

The labor force and the count of state residents working were little changed from late 2023 to late 2024, and the unemployment rate, which started 2024 at 4.8%, remained elevated relative to the national average, though an upward drift elsewhere and a tick down to 4.6% in New Jersey's rate at the end of the year eliminated much of the gap.

Mirroring the labor market gap with the national data, growth of the state's Gross Domestic Product and personal income have been somewhat below average, though growth has continued, and the state remains near the top for per capita output and income.

Data from New Jersey Realtors show that 2024 sales of single-family homes were little-changed from 2023, though sales prices continued to move up sharply, with the average nearly $700,000 in December. Prices in suburban New York counties are quite substantially higher than New Jersey's statewide average. Home building has grown modestly; U.S. Census Bureau permit numbers show some gains from 2023.

The Clouded Outlook

The economic outlook is extraordinarily uncertain. There have been some quite positive indications at the national level, most importantly the marked reduction in inflation, which allowed the Federal Reserve to lower its target interest rates. In addition, labor force productivity has been rather strong—whether that is the fruit of new technology remains to be seen. Finally, national job gains have remained robust, quite possibly reflecting a rebound in immigration swelling the labor force (though the sluggishness in New Jersey's labor force, despite what the Census Bureau reports as exceptionally high levels of international immigration to the state, is a bit at odds with this conclusion).

The uncertainty — which has apparently been reflected in substantive increases in long-term interest rates not under the Fed's control -- reflects the considerable uncertainty about what policies will ultimately be implemented by the new national administration, as well as their effects. The major concerns regard levying high tariffs and sharp restrictions on immigration (legal as well as undocumented).

Tariffs may spur a rebound in inflationary forces, spurring an end to Federal Reserve rate cuts or even leading to rate hikes. Foreign retaliation against U.S. tariffs would harm overseas sales by domestic industries. In addition, increased prices of foreign inputs which have no domestic counterparts could disrupt domestic production, offsetting any near-term spur to U.S. production from tariffs.

Uncertainty about the availability of labor in sectors such as construction and agriculture could also be disruptive, and it has also been suggested that there may be shortfalls in the numbers of highly trained immigrant workers in high-tech sectors.

Additionally changes in energy policy, while arguably rather neutral to the economy in the long run (discounting potential environmental and climate effects), could be sufficiently disruptive to be negatives in the short run.

Revenue Scenarios

The Multi-Year Budget Workgroup evaluated the revenue consequences of three scenarios: 1. Baseline, 2. Pessimistic, and 3. Optimistic. FY2024 and FY2025 revenue and expenditure figures reflect those in the FY2025 Appropriations Act.

The Baseline Scenario

The Baseline Scenario assumes that at least some of the tariff hikes will be implemented (and sustained) and that there will be a marked reduction in immigration. This is presumed to slow, though not halt, overall economic growth, while progress on reducing inflation will be arrested.

Consumer spending will slow as tariffs boost retail prices. Uncertainty will add volatility to financial markets, and in such an environment we assume the rate of capital gains realizations will slow.

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BASELINE SCENARIO							
Economic Assumptions and Revenue Projections							
	CY2023	CY2024	CY2025	CY2026	CY2027	CY2028	CY2029
National Outlook							
Real Gross Domestic Product Growth (% year over year)	2.9	2.8	1.8	1.5	2.1	2.0	2.0
Nominal Gross Domestic Product Growth (%)	6.6	5.3	4.9	4.5	4.1	4.0	4.0
Current Dollar Consumer Spending Growth (%)	6.4	5.3	4.5	3.5	4.1	4.0	4.0
Personal Income Growth (%)	5.9	5.4	4.5	4.0	4.0	4.0	4.0
Capital Gains Realizations (billions of dollars)	$1,250	$1,350	$1,400	$1,100	$1,100	$1,200	$1,300
Personal Income Plus Capital Gains Realizations Growth (%)	6.1	5.2	4.5	2.7	3.8	4.2	4.2
Consumer Price Index Growth (%)	4.1	3.0	2.7	3.0	2.8	2.5	2.5
Unemployment Rate (%)	3.6	4.0	4.4	4.7	4.5	4.2	4.2
New Jersey							
Taxable Consumer Spending Growth (%)	5.4	4.3	3.5	2.5	3.1	3.0	3.0
Personal Income Plus Capital Realizations Growth (%)	5.6	4.7	4.0	2.2	3.3	3.7	3.7
Unemployment Rate (%)	4.4	4.7	4.7	4.7	4.5	4.3	4.2
	FY2023	FY2024	FY2025	FY2026	FY2027	FY2028	FY2029
New Jersey State Budget Revenue Projections							
Sales and Use Tax (millions of dollars)	$13,981	$14,424	$14,699	$15,213	$15,594	$16,077	$16,560
Gross Income Tax Plus PT Business Alternative Income Tax (millions)	$23,160	$23,596	$24,036	$24,987	$25,535	$26,388	$27,363
Corporation Business Tax (millions)	$5,576	$5,347	$5,368	$5,921	$6,294	$6,438	$6,522
Other (millions)	$10,123	$9,434	$10,405	$10,400	$10,000	$10,200	$10,500
Total (millions)	**$52,840**	**$52,801**	**$54,508**	**$56,521**	**$57,422**	**$59,104**	**$60,945**

METHODOLOGY: FY2024 and FY2025 use Treasury assumptions for all taxes. Sales tax for FY2026-FY2029 calculated as increment by growth of taxable consumer spending in previous CY. Gross Income Tax and Pass Through Business Alternative Income Tax for FY2026-FY2029 calculated as increment by 227555.075 income plus capital gains realizations. Corporation Business Tax for FY2026-FY2029 calculated as increment by formula related to national nominal Gross Domestic Product growth. Corporation Business Tax includes energy and Corporate Transit Fee surcharge.

Assuming no further abrupt policy changes, this outlook has growth stabilizing after a year or so, though the trend will be lower than in recent years, in large part reflecting lesser immigration hampering the growth of the labor force. We put the odds on an outlook like this at roughly 45%.

The Pessimistic Scenario

The Pessimistic Scenario assumes much larger short-term policy effects, which push the economy into at least a mild recession later this year, continuing into 2026. A recovery follows, reflecting the likely Federal Reserve response to a weakened economy,

Federal tax and spending stimulus will also be likely, though concerns about debt levels may inhibit these, as well as some adjustment to the changed trade and immigration policy regime.

Such an outlook would put significant downward pressure on equity and real estate markets. We put the odds on such a scenario at roughly 40% (this includes the potential for much weaker outcomes).

PESSIMISTIC SCENARIO

Economic Assumptions and Revenue Projections

	CY2023	CY2024	CY2025	CY2026	CY2027	CY2028	CY2029
National Outlook							
Real Gross Domestic Product Growth (% year over year)	2.9	2.8	1.0	0.5	1.8	1.8	1.8
Nominal Gross Domestic Product Growth (%)	6.6	5.3	4.0	3.0	4.1	4.1	4.1
Current Dollar Consumer Spending Growth (%)	6.4	5.3	3.5	2.5	4.0	4.0	3.5
Personal Income Growth (%)	5.9	5.4	3.5	4.0	4.0	4.0	4.0
Capital Gains Realizations (billions of dollars)	$1,250	$1,350	$700	$500	$500	$550	$600
Personal Income Plus Capital Gains Realizations Growth (%)	5.6	2.6	2.6	2.7	3.9	4.1	4.1
Consumer Price Index Growth (%)	4.1	3.0	3.0	3	2.5	2.5	2.5
Unemployment Rate (%)	3.6	4.0	4.8	5.7	5.5	5.2	5.2
New Jersey							
Taxable Consumer Spending Growth (%)	5.4	4.3	2.5	1.5	3.0	3.0	2.5
Personal Income Plus Capital Realizations Growth (%)	5.1	2.1	2.1	2.2	3.4	3.6	3.6
Unemployment Rate (%)	4.4	4.7	4.8	5.7	5.5	5.2	5.2

	FY2023	FY2024	FY2025	FY2026	FY2027	FY2028	FY2029
New Jersey State Budget Revenue Projections							
Sales and Use Tax (millions of dollars)	$13,981	$14,424	$14,699	$15,067	$15,293	$15,751	$16,224
Gross Income Tax Plus PT Business Alternative Income Tax (millions)	$23,160	$23,596	$24,036	$24,546	$25,076	$25,936	$26,871
Corporation Business Tax (millions)	$5,576	$5,347	$5,368	$5,438	$4,965	$5,079	$5,196
Other (millions)	$10,123	$9,434	$10,405	$10,200	$9,800	$9,900	$10,100
Total (millions)	**$52,840**	**$52,801**	**$54,508**	**$55,250**	**$55,134**	**$56,666**	**$58,390**

METHODOLOGY: FY2024 and FY2025 use Treasury assumptions for all taxes. Sales tax for FY2026-FY2029 calculated as increment by growth of taxable consumer spending in previous CY. Gross Income Tax and Pass Through Business Alternative Income Tax for FY2026-FY2029 calculated as increment by growth of personal income plus capital gains realizations. Corporation Business Tax for FY2026-FY2029 calculated as increment by formula related to national nominal Gross Domestic Product growth. Corporation Business Tax includes energy and Corporate Transit Fee surcharge.

The Optimistic Scenario

The Optimistic Scenario assumes that the actual policies implemented will be fairly modest, and that growth will continue close to recent trends. We put the odds on this at only 15%.

Under the Baseline Scenario, state revenue growth will be around 2 to 4 percent a year through FY29.

In the Pessimistic Scenario, revenues will be basically flat in FY26 and FY27, and even with growth resuming, will be more than $3 billion below the baseline in FY29.

The Optimistic Scenario sees state revenues in FY29 nearly $2 billion higher than the baseline, and about $5 billion above the pessimistic projection.

OPTIMISTIC SCENARIO							
Economic Assumptions and Revenue Projections							
	2023	2024	2025	2026	2027	2028	2029
National Outlook							
Real Gross Domestic Product Growth (% year over year)	2.9	2.8	2.6	2.3	2.1	2.0	2.0
Nominal Gross Domestic Product Growth (%)	6.6	5.3	4.9	4.5	4.1	4.0	4.0
Current Dollar Consumer Spending Growth (%)	6.4	5.3	4.7	4.3	4.1	4.0	4.0
Personal Income Growth (%)	5.9	5.4	4.3	4.6	4.0	4.0	4.0
Capital Gains Realizations (billions of dollars)	$1,250	$1,350	$1,400	$1,450	$1,500	$1,550	$1,600
Personal Income Plus Capital Gains Realizations Growth (%)	6.1	5.2	4.3	4.5	4.0	4.0	4.0
Consumer Price Index Growth (%)	4.1	3.0	2.7	2.5	2.5	2.5	2.5
Unemployment Rate (%)	3.6	4.0	4.0	4.0	4.0	4.0	4.0
New Jersey							
Taxable Consumer Spending Growth (%)	5.4	4.3	3.7	3.3	3.1	3.0	3.0
Personal Income Plus Capital Realizations Growth (%)	5.6	4.7	3.8	4.0	3.5	3.5	3.5
Unemployment Rate (%)	4.4	4.7	4.2	4.1	4.0	4.0	4.0
	FY2023	FY2024	FY2025	FY2026	FY2027	FY2028	FY2029
New Jersey State Budget Revenue Projections							
Sales and Use Tax (millions of dollars)	$13,981	$14,424	$14,699	$15,243	$15,746	$16,234	$16,721
Gross Income Tax Plus PT Business Alternative Income Tax (millions)	$23,160	$23,596	$24,036	$24,942	$25,951	$26,852	$27,783
Corporation Business Tax (millions)	$5,576	$5,347	$5,368	$5,921	$6,294	$6,438	$6,522
Other (millions)	$10,123	$9,414	$10,405	$10,700	$10,900	$11,100	$11,400
Total (millions)	**$52,840**	**$52,801**	**$54,508**	**$56,805**	**$58,891**	**$60,625**	**$62,426**

METHODOLOGY: FY2024 and FY2025 use Treasury assumptions for all taxes. Sales tax for FY2026-FY2029 calculated as increment by growth of taxable consumer spending in previous CY. Gross Income Tax and Pass Through Business Alternative Income Tax for FY2026-FY2029 calculated as increment by 230828.7984 income plus capital gains realizations. Corporation Business Tax for FY2026-FY2029 calculated as increment by formula related to national nominal Gross Domestic Product growth. Corporation Business Tax includes energy and Corporate Transit Fee surcharge.

Current Services Budget

The Current Services Budget for FY26 to FY29 is a baseline spending plan that shows the projected costs of continuing state services and state aid at current levels with normal inflation, along with the cost of major spending commitments made by the Governor and Legislature. These include full funding of state education aid, continued full actuarial pension payments, continued implementation of the StayNJ property tax credit, and dedicated funding of NJ Transit through the corporation business tax surcharge enacted last June.

Our Current Services Budget differs from a true Multi-Year Budget that would include recommendations for major policy changes in the years ahead to improve services, cut costs and meet policy priorities. While our revenue forecasts are identical to those that would be required under Senate Bill 654, our Current Services Budget is similar in approach, though less detailed, than the document that would have been required under the Oroho-Sarlo consensus revenue forecasting legislation.

Like the 2010 *Facing Our Future* report that was the last to provide a five-year current services projection for the state budget prior to the Multi-Year Budget Workgroup studies we issued in 2022, 2023 and 2024, our Current Services Budget for FY25 to FY29 provides an aggregate picture at the macro level in major spending areas, particularly those programs that make up large cost centers or have been the subject of large increases.

Over the past seven fiscal years, budget expenditures rose from $34.7 billion in FY2018 to $56.6 billion in the current FY2024 budget year. In addition to normal inflationary increases, the rise in expenditures was driven by a $6 billion increase in state aid to education under the School Funding Fairness Act of 2018, a $5 billion ramp-up to the full Actuarially Required Contribution to the state pension system for teachers and state workers that had been underfunded for more than 20 years, and implementation of the new $2 billion ANCHOR property tax relief program.

Overall state expenditures – including federal aid, the Transportation Trust Fund, and revolving and dedicated funds that provide funding in addition to the $56.6 billion supported by state revenues – grew with equal rapidity. In response to the Covid crisis, federal funding jumped from $13.9 billion in FY19 to $16.3 billion in FY20 and peaked at $23.billion in FY23 and was projected to come in at $22.4 billion for the current fiscal year.

Those federal aid numbers – both in the current budget and for future budgets – are the biggest question marks that will face state budget makers in the months ahead, as the Trump Administration moves to cut the federal workforce and freeze grant funding and Congress weighs deep cuts to Medicaid as part of its plan to pay for continued tax cuts.

Fifteen percent of the state government workforce is federally funded, and $17.4 billion in federal aid goes to the state Departments of Human Services, Health, Children and Families, and Military and Veterans Affairs to fund hospital and health care costs for 1.8 million lower-income and disabled citizens covered by NJ Family Care/Medicaid, to pay for care in the state's psychiatric hospitals, developmental centers and veterans homes, and to support various child protection and social service programs.

Proposed cuts in research-and-development grants to universities, a threatened freeze in grants to non-profits and other yet-to-be-determined federal cuts are also likely to put pressure on New Jersey state budget-makers to provide additional funding to bridge the gap and avert layoffs.

The impact of cuts authorized by federal executive orders or carried out by the federal Department of Government Efficiency is likely to be clear by the June 30 state budget deadline, but it is possible that congressional cuts to Medicaid will not be finalized before the September 30 federal budget deadline, necessitating major mid-year budget adjustments before the November election for Governor and Assembly.

None of those potential cuts are included in the Current Services Budget.

Overall, we now project Current Services Budget expenditures to rise $8.6 billion over the next four fiscal years from $56.6 billion in FY25 to $65.3 billion in FY29. With Trump Administration tariff and deportation policies fueling economic uncertainty and increasing the likelihood of a mild recession, state revenues are projected to fall $2.2 billion to $6.7 billion short of the amount needed to fund projected Current Services Budget costs each year from FY26 to FY29 under all three MYBW revenue scenarios.

It is important to note that this $8.6 billion increase does not include the $600 million in one-shot targeted budget add-ons for specific towns, districts, colleges, non-profits and programs in the FY25 budget that we took out of the base Current Services Budget for the purpose of calculating future spending; this is an important change in methodology we decided to make last year because the so-called "Christmas tree list" changes from year to year and has been virtually eliminated in years of fiscal crisis.

Four increases in our projected Current Services Budget over the next four fiscal years account for over 80% of the aggregate $22.3 billion total increase in state spending over that time: (1) healthcare costs, (2) state aid to education, (3) property tax relief and (4) NJ Transit operations.

Health Care Costs

Based on the federal Centers for Medicare and Medicaid Services (CMMS) healthcare inflation multiplier of 5.1%, we project that state spending for the Department of Human Services, including Medicaid, and for public employee and retiree health benefits will grow from $14 billion in FY2025 to $17 billion by FY2029. The $7.5 billion aggregate increase for these

PROJECTED CURRENT SERVICES BUDGET

Human Services, Medicaid, DMAVA vetrans homes and health benefit spending projected at 5.1% growth from FY25 to FY29 using federal CMMS multiplier. Pension costs are actuarial projections from state bond offering. Corporate Transit Fee (CBT surcharge) dedicated to NJ Transit in FY26-FY29 to fill projected gap after exhaustion of federal Covid-19 subsidy funding in FY25; surcharge was applied to General Fund in FY25. StayNJ fully funded in accordance with law. Targeted $600 million in one-shot appropriations for FY25 not included in Current Services Budget for following year. School aid and all other spending increased 3% annually for inflation, except for debt service, which is kept flat.

	FY22 Actual Expenditure	FY23 Actual Expenditure	FY24 Actual Expenditure	FY25 Actual Appropriation	FY26 Projected Appropriation	FY27 Projected Appropriation	FY28 Projected Appropriation	FY29 Projected Appropriation
TOTAL NJ STATE BUDGET APPROPRIATIONS								
Projected Current Services Budget	**$48,787,000**	**$54,642,000**	**$55,501,000**	**$56,613,821**	**$58,821,281**	**$61,460,266**	**$63,274,751**	**$65,233,961**
Projected Percent Increase				2.01%	3.90%	4.49%	2.95%	3.10%
MAJOR SPENDING INCREASES								
Previously Committed Spending Growth								
1. Pre K-12 State Aid to School Districts	$10,200,000	**$10,828,495**	**$11,766,276**	**$12,793,994**	**$13,177,814**	**$13,573,148**	**$13,980,343**	$14,399,753
2. Direct Property Tax Relief Programs								
ANCHOR, Senior Freeze, other direct property tax relief	$617,900	$2,248,300	$2,479,400	$2,506,600	$2,513,679	$2,520,777	$2,527,896	$2,599,283.72
StayNJ program			$102,000	$220,000	$300,000	$1,200,000	$1,224,000	$1,248,480.00
Total Direct Property Tax Relief in Budget		**$2,248,300**	**$2,581,400**	**$2,726,600**	**$2,813,679**	**$3,720,777**	**$3,751,896**	**$3,847,764**
3. Medicaid/Healthcare Cost Increases								
a. Department of Human Services	**$7,040,291**	**$8,307,958**	**$9,212,229**	**$9,848,831**	**$10,205,502**	**$10,725,983**	**$11,273,008**	**$11,847,931**
b. Public Employee Health Benefits								
Health Benefits for Current State Employees	$1,496,364	$1,677,764	$1,788,702	$1,830,247	$1,923,589.60	$2,021,692.67	$2,124,798.99	**$2,233,164**
Medical Benefits for Retired Teachers, State Employees	$1,946,460	$2,113,587	$2,316,734	$2,394,967	$2,517,110.32	$2,645,482.94	$2,780,402.57	**$2,922,203**
Health Benefits Total, Active and Retirees	**$3,396,342**	**$3,791,351**	**$4,105,436**	**$4,225,214**	**$4,440,700**	**$4,667,176**	**$4,905,202**	**$5,155,367**
c. DMAVA Veterans Nursing Homes	**$67,888**	**$70,645**	**$87,985**	**$88,899**	**$93,433**	**$98,198**	**$103,206**	**$108,470**
4. NJ Transit Post-Covid Funding Operating Deficit								
NJ Transit Budget	**$2,678,100**	**$2,710,500**	**$2,868,613**	**$3,003,503**	**$3,099,200**	**$3,192,176**	**$3,287,941**	**$3,386,579.5**
NJ Turnpike Funding	$325,000	$721,000	$440,000	$455,000	$470,000	$484,100	$500,000	$500,000
NJ Transit State Operating Subsidy	$100,000	$100,000	$142,000	$145,000	$145,000	$145,000	$145,000	$145,000
Farebox Revenue	$536,700	$696,800	$785,300	$947,000	$1,005,000	$1,035,150	$1,066,205	$1,098,190.6
Capital to Operating Transfers, Clean Energy Fund, Misc.	$835,900	$801,400	$730,400	$707,200	$712,400	$717,600	$772,800	$729,000
Covid-19 Relief (CARES, CRRSAA, ARPA)	$1,030,800	479,300	$808,800	$749,300	$0	$0	$0	0
NJT Revenue -to-Expenditure Differential	**$150,300**	($4)	**$0**	**$0**	**($766,800)**	**($810,326)**	**($853,907)**	**($914,389)**
Corporate Transit Fee (CBT surcharge) covers gap					**$766,800**	**$810,326**	**$853,937**	**$914,389**
MAJOR EXPENDITURES PROJECTED AT NO GROWTH OR BELOW 3%								
1. Pension Contribution from State Budget								
State Pension Contribution	$5,797,000	$5,719,000	$5,971,000	$6,036,000	$5,822,000	$5,878,000	$5,923,000	5,963,000
State Lottery Contribution	$1,111,000	$1,170,000	$1,116,000	$1,126,000	$1,135,000	$1,147,000	$1,157,000	1168000
Total State Pension Funding	**$6,908,000**	**$6,889,000**	**$7,087,000**	**$7,162,000**	**$6,957,000**	**$7,025,000**	**$7,080,000**	**$7,131,000**
2. Debt Service	**$4,352,900**	**$4,459,300**	**$4,155,000**	**$4,444,569**	**$4,444,569**	**$4,444,569**	**$4,444,569**	**$4,444,569**
3. Targeted One-Shot Expenditures (excluded from CSB)			**$926,000**	$600,000				
4. Health Care Accessibility and Affordability Fund (Horizon Payment)		**$600,000**	**$100,000**					
Subtotal for State Expenditures Detailed	$32,065,421	$37,295,049	$39,375,879	$41,296,554	$43,044,496	$45,210,177	$46,537,160	$47,994,242
Expenditures not listed (3% growth factored in FY26-FY2!	$16,721,579	$17,346,951	$16,125,121	$15,317,267	$15,776,785	$16,250,089	$16,737,591	$17,239,719
Total Current Services Budget	**$48,787,000**	**$54,642,000**	**$55,501,000**	**$56,613,821**	**$58,821,281**	**$61,460,266**	**$63,274,751**	**$65,233,961**

healthcare costs makes up almost one third of the total projected increase for the state budget over the four-year period. It is also the number most likely to increase.

New Jersey Medicaid enrollment peaked at 2.3 million before the April 1, 2023, end of the Covid-19 Public Health Emergency required the state Department of Human Services to “unwind” expanded coverage rules that had been in place since March 2020. Enrollment has now flattened at 1.8 million, so future growth will be driven primarily by increases in the cost of services. The National Health Expenditures Account projects 5.7% growth over the next four years, partly because the departure of healthier enrollments from the program leaves a more costly case mix than before disenrollments began.

Medicaid growth is primarily dependent on two variables – economic conditions and federal policy. Poorer economic conditions historically have caused an increase in enrollment. More importantly, federal policy changes could result in substantial reductions in Federal Medicaid funding. One potential change that could gain traction would include reducing the 90% federal match included as part of the Affordable Care Act for states that expanded Medicaid to 50% and then instead provide block grants (in roughly the same amount as the 40% they took by reducing the match) for states to finance coverage expansions as they choose – this would level the playing field for the 10 states that still have not expanded Medicaid.

The Governor’s budget for FY2026 is also likely to show an increase in state health benefits costs higher than the 5.1% CMMS multiplier, based on the State Health Benefit Plan’s approval of a 10.6% rate increase for active employees and 10.9% for retirees for calendar year 2025, which spans the current FY2025 and upcoming FY2026 budgets.

State Aid to Education

State aid to education under the School Funding Reform Act formula, which is the largest single spending item in the budget, rose from $11.77 billion in FY24 to $12.79 billion in the FY25 budget, as the Governor and Legislature completed the ramp-up to full funding of the S2 school funding formula established under the School Funding Fairness Reform Act of 2018. With the ramp-up complete, state aid to education is projected to rise just 3% annually in future years to $14.4 billion, but the cumulative four-year increase will still total $3.955 billion.

Property Tax Relief

The StayNJ program and the expansion of the ANCHOR program are projected to grow from $2.67 billion to $3.85 billion in Current Services Budget scenario costs over the four fiscal years, with the biggest single-year cost increase of $900 million for StayNJ coming in the FY2027 budget that would be the first enacted by the new Governor and Assembly elected in November 2025. The StayNJ program, combined with the other programs, would provide

50% property tax cuts up to a maximum of $6,500 for senior citizens and the disabled starting in FY2027. The projected FY2026 cost is $300 million, an $80 million increase over this year's $220 million appropriation. With funding set aside the two previous years, seniors and the disabled would receive a StayNJ half-payment up to $3,250 in the spring of 2026. Overall, StayNJ will add almost $3.1 billion in costs to the state's property tax relief programs from FY2025 to FY2029.

NJ Transit

We project that the state budget, which already provides a $145 million operating subsidy to NJ Transit out of general funds, will provide an additional $766.8 million in FY2026, $810.3 million in FY2027, $853.9 million in FY2028 and $914 million in FY2029 to cover the fiscal cliff created now that the agency's federal Covid-19 operating assistance money has fully run out. These numbers are based on the four-year projections in NJ Transit's FY2025 multi-year budget. This additional funding is projected to come from a dedicated Corporate Transit Fee funded by an increase in the Corporate Business Tax on companies earning over $10 million a year in profits in. New Jersey. The Governor and Legislature used the $1.023 billion projected to be generated by the new CBT surcharge as a one-shot revenue to balance the overall state budget in FY2025, exacerbating the fiscal cliff in the upcoming FY2026 budget. The total increase in state subsidies for NJ Transit is projected at $3.3 billion over four years. NJ Transit's operating subsidy for FY25 also included $455 million from the New Jersey Turnpike Authority, a subsidy that is projected to rise to $500 million by FY2028.

Pensions and Debt Service

These major increases are offset partially by virtually flat funding for the state's pension system now that the full Actuarially Required Contribution is being made each year; by flat debt service payments despite relatively high interest rates because of past expenditures from the Debt Defeasance Fund; and by the expected continuation of flat funding for municipal aid, which has been frozen at less than $1.6 billion for more than two decades. All other spending is calculated to grow at a 3% annual rate.

Appendix A

Five-Year Revenue Forecast Assumptions and Methodology

Revenue Projections

For purposes of projection, New Jersey state revenues are placed into 4 categories:

1. Personal income taxes, consisting of the Gross Income Tax (GIT) and the Business Alternative Income Tax (BAIT). The BAIT, which is fully deductible against federal tax liabilities, can be credited against either the GIT or the Corporate Business Tax (CBT), but since its recent promulgation, experience suggests that it can be viewed as essentially an alternate way to pay GIT liabilities.
2. Corporate taxes, consisting of the CBT plus the separately reported taxes on energy and financial corporations.
3. Sales taxes, consisting of the Sales and Use Tax (SUT) plus the separately reported energy component.
4. All other revenues, consisting of a wide variety of taxes and fees. These include real estate transaction taxes, taxes on insurance premiums, lodging, motor fuels, tobacco products and marijuana sales, casino gaming revenues, and alcohol, as well as the transfer inheritance tax and motor vehicle license fees.

Personal income and sales taxes account for the largest share of revenues, followed distantly by corporate taxes (these have often been referred to as the "Big 3'). Personal and corporate income tax revenues are notoriously volatile. However, due to its much larger size, errors in the certified projections for income taxes have been historically more consequential for overall state revenues than those for corporate taxes, even though corporate tax revenues are more volatile.

Determinants of Revenues

Aside from policy changes, revenue growth is essentially determined by New Jersey's economy. In turn, since New Jersey is a large economically diverse state, changes in the national economy can be a significant determinant of New Jersey's economic performance. Medium-term changes in New Jersey's revenues (again barring significant policy changes) are generally reflective of changes in the national economy over that period.

Personal Income Taxes

A reasonable proxy for the growth of New Jersey's taxable income base for a fiscal year is the growth of the state's personal income in the previous calendar year, plus capital gains realizations by state residents.[1] Based on an analysis of available data, New Jersey's growth of its personal income base tends to be about a half percent a year less than the nation as a whole. Large movements in the capital gains proportion will have significant implications for New Jersey income tax revenue, given the pronounced progressivity of New Jersey income tax rates, and the disproportionate share of capital gains realizations earned by households in high income brackets.

Corporate Taxes

The exact relationship, even at the national level, between corporate tax receipts and economic activity is hard to pin down, due to the frequent changes in tax policy. We assume that in the medium-term New Jersey's corporate tax revenues in a fiscal year will be related to the growth of national pre-tax operating earnings in the previous calendar year.[2] We also assume that these earnings will typically grow faster than current-dollar (nominal) Growth Domestic Product (GDP), given the trends of the last generation. If GDP grows faster than usual, the corporate tax base will grow even faster.[3] Likewise, profit growth will be much slower when GDP grows less than average.

Under any scenario or set of assumptions, the projection of corporate revenues is likely to be uncertain, given the wide divergence between New Jersey corporate tax rules and those of other states and the federal government. An error band of as much as $1 billion—or close to 20 percent of New Jersey corporate tax revenue earned in recent years—is conceivable around any projection, even if all elements of the economic projection are correct. We believe that the risks are weighted to the downside, given the unique nature of New Jersey's corporate tax system and the unanticipated surge in revenues in recent years.

Sales Taxes

Although New Jersey collects sales tax on some forms of business-to-business transactions, more than half of the revenue comes from retail purchases. US Bureau of Economic Analysis data suggest that annual growth of spending in New Jersey on taxable items is typically about 1 percentage point less than national aggregate consumer spending, based on annual business expense data. The divergence reflects not only slower population and economic growth in New Jersey but also the tendency for consumer spending to shift to nontaxable services such as housing, health care, and education. We assume that sales tax growth in a fiscal year will be one percent slower than growth in national (current-dollar) consumer spending in the prior year.

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[1] Timely New Jersey personal income figures are available from the US Bureau of Economic Analysis. Our estimates and projections for capital gains realizations in recent years are based on the latest available IRS data for the nation as a whole, as well as Treasury reports and testimony.

[2] Pre-tax operating earnings are profits with inventory valuation and capital consumption adjustments.

[3] We assume 10 percent more for every percent of more rapid GDP growth.

Other Revenues

Some taxes in this group—most notably real estate transaction taxes, but also lodging taxes—clearly do reflect economic conditions, while the transfer-inheritance tax is more responsive to market swings which affect the value of estates. Other taxes, however, have little or no clear trends (motor vehicle license fees, for instance); others are determined by fairly complex mechanisms (casino revenues, motor fuel, cigarette taxes, etc.). The recent surge in home sales has been a major factor in collecting more than $9 billion in miscellaneous revenue (exclusive of the FY2021 receipt of emergency COVID borrowing). Our baseline assumes that going forward these receipts will generally equal the average of the previous 5 fiscal years (again, not taking into account the FY2021 borrowing, as well as the Horizon transaction), though we anticipate that the recent surge in real estate transaction revenues will roll back and anticipate that the state will realize less in investment earnings from its surplus than the large sums assumed for Fiscal years 2023 and 2024.

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